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The Criminalization of Questionable Foreign Payments by Corporations: A Comparative Legal Systems Analysis

Gerald T. McLaughlin

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Cover Page Footnote

Professor, Fordham University School of Law. The author wishes to express his sincere appreciation to Gerald Garlick of the Georgetown University Law School for his invaluable assistance in the preparation of this Article.

THE CRIMINALIZATION OF QUESTIONABLE FOREIGN PAYMENTS BY CORPORATIONS: A COMPARATIVE LEGAL SYSTEMS ANALYSIS

GERALD T. McLAUGHLIN*

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I. INTRODUCTION

Recently an Ad Hoc Committee of the Association of the Bar of the City of New York wrote: "No single issue of corporate behavior has engendered in recent times as much discussion in the United States—both in the private and public arenas—and as much administrative and legislative activity, as payments made abroad by corporations."¹

Although payments by such corporate giants as Lockheed,² Exxon,³ and Northrop⁴ have received the most extensive press coverage, the practice has not been confined to the giants alone. More than 400 corporations, over 117 of them in the top Fortune 500, have admitted making questionable or illegal payments.⁵ In total, these corporate payments have exceeded 300 million dollars.⁶ Among other things, their disclosure has forced the removal of a Central American president,⁷ embarrassed a Philippine regime,⁸ led to a constitutional crisis in the Netherlands,⁹ caused legislative paralysis in Japan,¹⁰ and shaken an Italian government.¹¹ In the United States, questions over the propriety of foreign payments recently delayed the confirmation of the chairman of the Federal Reserve Board.¹²

Responding to such revelations, Congress recently enacted the Foreign Corrupt Practices Act of 1977 prohibiting corporations from making

use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to—

1. Association of the Bar of the City of New York, Report on Questionable Foreign Payments by Corporations: The Problem and Approaches to a Solution 1 (1977) [hereinafter cited as Report of the Bar of the City of New York]. Questionable payments provided a "rich source of new business" for Wall Street lawyers. Bernstein, *The Wall Street Lawyers Are Thriving on Change*, Fortune, Mar. 13, 1978, at 107. The complexities of the issues have occasionally driven the legal fees in excess of the questionable payments. See *id.*

2. See, e.g., Lindsey, *A Bribery Scandal—The Give and the Take*, N.Y. Times, July 3, 1977, § 3, at 1, col. 1.

3. See, e.g., N.Y. Times, Feb. 10, 1974, at 6, col. 1.

4. See, e.g., Jensen, *U.S. Company Payoffs: Way of Life Overseas*, N.Y. Times, May 5, 1975, at 1, col. 1.

5. House Comm. on Interstate and Foreign Commerce, Unlawful Corporate Payments Act of 1977, H.R. Rep. No. 640, 95th Cong., 1st Sess. 4 (1977).

6. *Id.*

7. N.Y. Times, Apr. 23, 1975, at 1, col. 1.

8. *Id.*, Jan. 14, 1978, at 1, col. 2.

9. See *id.*, Feb. 9, 1976, at 1, col. 5.

10. *Id.*, Apr. 19, 1976, at 15, col. 1.

11. *Id.*, Apr. 23, 1976, at 1, col. 4.

12. *Id.*, Feb. 24, 1978, at 1, col. 1. The Senate, however, ultimately confirmed G. William Miller with only one dissenting voice. *Id.*, Mar. 4, 1978, at 27, col. 3.

- (1) any foreign official for purposes of—
 (A) influencing any act or decision of such foreign official in his official capacity . . . or
 (B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality, in order to assist [such corporation] in obtaining or retaining business for or with, or directing business to, any person¹³

The statute defines "foreign official" as "any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or any person acting in an official capacity for or on behalf of such government or department, agency, or instrumentality."¹⁴ The term does not include "any employee of a foreign government or any department, agency, or instrumentality thereof whose duties are essentially ministerial or clerical."¹⁵

Corporations violating the new statute face a possible fine of up to one million dollars¹⁶—one of the stiffest in the United States Criminal Code. By requiring that the payments be made to foreign officials for

13. Foreign Corrupt Practices Act of 1977, Pub. L. No. 95-213, § 104, 91 Stat. 1496 (1977) (to be codified at 15 U.S.C. §§ 78a-78o) [hereinafter cited as Foreign Corrupt Practices Act]. The legislation amends the Securities Exchange Act of 1934 to forbid "issuers" from making these payments and then enacts new legislation prohibiting "domestic concerns" (non-issuers) from making such payments. The definition of "domestic concern" includes individuals, however. Questionable foreign payments by corporations might be broken down into four distinct categories: (a) the outright bribe—a payment used to influence an official's discretionary act, or to encourage an official to do an unlawful act; (b) a "grease" payment—a payment made to ensure that an official will perform a nondiscretionary act or perform it within a reasonable time; (c) the goodwill payment—a payment made with no specific policy decision in mind, but to assure a reservoir of benevolence vis-à-vis the company at some future time; and (d) a political contribution—a variety of goodwill payment—made to a political candidate or party. Often, however, payments cannot be neatly fit into one or another of the four categories. If a company knows, for example, that a new contract with a particular government may be in the offing, would a payment to the government official in charge of deciding who receives government contracts be a goodwill payment or a form of bribe? Since nothing is being asked in return for the money, it could be viewed as a goodwill payment. Yet it is so closely connected to an upcoming discretionary policy decision that it has the overtones of a bribe.

The new legislation criminalizes the bribe and the political contribution but does not criminalize the "grease" payment. As for the goodwill payment, it would seem that the legislation can be read as criminalizing this form of payment. The goodwill payment is made to influence future acts of the government. The quid pro quo, although deferred, is still expected to be given.

The proposed revision of the United States Criminal Code would no longer include "corruptly" as a culpable state of mind. See S. 1437, 95th Cong., 2d Sess. § 301, at 32 (1978). Foreign corporate payments apparently would be criminalized under § 1351(a) of the revised Code because the definition of public servant seems to include an official of a foreign government. See *id.* § 111, at 14 ("public servant" and "government").

14. Foreign Corrupt Practices Act, § 30A(b) (to be codified at 15 U.S.C. § 78dd(1)(b)).

15. *Id.*

16. *Id.* § 104(b)(1)(A) (to be codified at 15 U.S.C. § 78dd(2)(b)(1)(A)).

the purpose of obtaining business, and by excluding clerical employees of a foreign government from the definition of "foreign official," Congress intended to distinguish between outright bribes—payments which cause an official to exercise other than his free will in acting or in making a decision—and so-called "facilitating" or "grease" payments—payments which merely move a particular matter toward an eventual act or decision, or which do not involve any discretionary action.¹⁷ In criminalizing the bribe but not the "grease" payment, Congress has seemingly made a limited accommodation to the realities of foreign business practices. But Congress refused to make any further accommodations, criminalizing all payments whose purpose was to influence discretionary governmental action whenever and wherever made. This Article will argue that because of the structural differences among legal systems, the broad based criminalization approach adopted by Congress may not be well advised.

"May not be well advised" is used because this Article does not attempt to deal with all of the policy reasons supporting criminalization of questionable payments. For example, moral or foreign policy considerations might tip the balance in favor of criminalization. This Article argues only that from the perspective of a comparative legal systems analysis, criminalization does not appear to be the wisest course.

In order to develop the argument against criminalization, Part II of this Article will first suggest a structural model of the American legal system—*i.e.* that of a legal system where governmental power, whether executive or legislative, is not absolute, and where both an independent judiciary with the power of judicial review and constitutional protections exist to curb any arbitrary or capricious exercise of that governmental power.¹⁸ The Article will then argue that this structural model is not necessarily present in other legal systems. Because of these structural dissimilarities among legal systems, this Article will suggest that criminalizing questionable payments may be an unwise course of action for two reasons. First, the structural differences among legal systems will make it more difficult to prove that payments are "corruptly" made. Second, questionable payments may represent a form of compensating mechanism for the lack of strong judicial and constitutional protections in certain legal systems whose structural model is different from that of the United States.¹⁹

17. See Senate Comm. on Banking, Housing, and Urban Affairs, *Foreign Corrupt Practices and Domestic and Foreign Investment Improper Disclosure Acts of 1977*, S. Rep. No. 114, 95th Cong. 1st Sess. 10, reprinted in [1977] U.S. Code Cong. & Ad. News 6306 [hereinafter cited as Senate Report].

18. See pt. II(A) *infra*.

19. See pt. II(B) *infra*.

Part III of the Article will then turn to an analysis of other American legislation which has an impact on the question of foreign corporate payments.²⁰ It will suggest that the lessons learned from the comparative legal systems analysis in Part II may also be valuable in determining the manner in which these other statutes should be enforced.

II. A COMPARISON OF LEGAL SYSTEM MODELS

At the outset the reader is asked to accept the following model of the American legal system. It is a legal system where neither the executive nor the legislative branches of government are autonomous;²¹ it is a legal system where an independent judiciary with the power of judicial review exists;²² and it is a legal system where there are meaningful constitutional protections against arbitrary government action.²³

In such a system, the courts and constitution require the executive and legislative branches of government to make principled (*i.e.* non-arbitrary) decisions with respect to the foreign investor. Thus, in the American model, criminalizing questionable payments to government officials can be justified. Where structural mechanisms (*i.e.* the courts and a constitution) restrict the government from acting arbitrarily or capriciously, the payment will be more likely to be "corruptly" made—that is, made with the specific intent to influence the government to select from among a range of discretionary but reasonable alternatives, the one most advantageous to the investor.²⁴ But it is necessary to compare the model of the American legal system with those in other areas of the world to see first, whether there are significant variants in structure among legal systems and second, if there are, how these

20. See pt. III *infra*.

21. For example, the President can veto an act of Congress but the veto can be overridden by a two-thirds vote of both Houses. U.S. Const. art. I, § 7, cl. 2.

22. Article III of the Constitution of the United States establishes a federal judiciary separate and apart from the legislative and executive branches. U.S. Const. art. III. Although federal judges are appointed by the President with the advice and consent of the Senate, they hold office during good behavior and can only be removed by impeachment. They are thus afforded a large measure of independence from the other branches of government. On the federal courts' power of judicial review of the acts of the legislature, see *Marbury v. Madison*, 5 U.S. (1 Cranch) 137 (1803), and on the executive, see *United States v. Nixon*, 418 U.S. 683 (1974). Similar protections giving the state judiciary independence can be found in various state constitutions.

23. For example, the fifth amendment of the Constitution of the United States states: "[N]or [shall any person] be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use, without just compensation." U.S. Const. amend. V. See also U.S. Const. amend. XIV.

24. For a discussion of the degree of culpability needed for proving that a payment of money was "corruptly" made under the federal bribery statute, 18 U.S.C. § 201(c)(1) (1970), see *United States v. Brewster*, 506 F.2d 62, 71-73 (D.C. Cir. 1974).

variants impact on the question of whether to criminalize questionable payments.

A. *Structural Differences*

It is, of course, impossible in an Article of this limited length to compare the American model with all other existing legal models. Consequently, it will be necessary to focus the analysis on one legal model to the exclusion of others. The civil law models of Europe or Latin America or the Japanese legal model would have provided fruitful fields for comparison—particularly in light of the reported payments made in these areas.²⁵ The author, however, has selected the Middle East legal model as his focus, chiefly for three reasons. First, in recent decades the Middle East has become an increasingly important area of the world, both politically and financially. Second, the most cursory glance reveals that Middle Eastern culture and legal traditions are markedly dissimilar from our own, thus giving a sharper focus to the comparative analysis. Third, although by no means the only part of the world where questionable payments have been reported, these payments do not seem to have been an uncommon phenomenon in the area.²⁶ In comparing the structure of the American legal model with that of the Middle East, however, one caveat must be kept in mind. By analyzing as a whole one legal tradition which covers so vast a geographic area and so many different countries,²⁷ the reader must be aware that some over-generalization is inevitable. What may be true in Saudi Arabia may be more or less true in Egypt or Iran. The purpose of the analysis is not to show the precise differences between the American legal system and the legal system of any one Middle Eastern country; rather it is to show that, *in its most general structure*, the Middle Eastern legal model appears significantly different in relevant respects from our own.

1. Executive Autonomy

The first constitutive element of the American model relates to the power of the legislative and executive branches of the government. In

25. See notes 7, 9-11 *supra*. For a discussion of questionable payments made in Chile and Colombia, see Report to the Shareholders of the General Tire Company, July 19, 1977, at 4 and Time, Feb. 23, 1976, at 28. See also N.Y. Times, Feb. 5, 1976, at 1, col. 5; *id.*, Mar. 3, 1977, at 46, col. 5.

26. See, e.g., N.Y. Times, Mar. 31, 1978, § D, at 1, col. 2; Wash. Post, July 20, 1977, § D, at 7, col. 1. See also *Multinational Corporations and United States Foreign Policy, Hearings before the Subcomm. on Multinational Corporations of the Senate Comm. on Foreign Relations*, 94th Cong., 1st Sess. 848-49 (1975) [hereinafter cited as *Senate Subcommittee Hearings*].

27. For an acceptable definition of the Middle East, see R. Patai, *The Arab Mind* 10-11 (1973).

the American system, neither the executive nor the legislature has absolute power. In the Muslim legal tradition, however, the opposite is more nearly correct. Although the Muslim ruler was theoretically bound by the *Sharia*, or sacred law of Islam, in practice the *Sharia* seems to have made him virtually autonomous: first by accepting de facto political power as de jure political power, and second by rejecting the right of the community to revolt against anyone who holds political power. Although the subject is a vast and complicated one, some brief discussion must necessarily be given to each of these separate points.

a. The Legitimacy of Acquiring Power

In the United States, for almost two hundred years, political power has been transferred pursuant to constitutional mandate. The legitimacy of any American government can always be tested by these fundamental constitutional principles. Islam, however, never stressed one particular form or method of transferring power. In classical Islamic legal theory, the Caliph or successor of the Prophet of God was the chief executive officer of the Islamic community.²⁸ To him was entrusted the defense and maintenance of the *Sharia*²⁹ and from him was delegated power to govern the various regions of Islam.³⁰ The Koran, however, did not specify how the Caliphate was to be acquired or transferred. Mohammed himself did not address the question—in fact, he did not even appoint a successor. The first Caliph, Abu Bakr, was chosen in the traditional fashion of an Arab chieftain—election by the leading men of the community.³¹ Before he died, however, Abu Bakr appointed a successor, Umar, as the second Caliph.³² In his turn, Umar refused to appoint a successor in the manner of Mohammed and Uthman was elected.³³ Ali, the fourth Caliph, was also elected³⁴ but his successor Mu'awiyah took the office by force of arms.³⁵ Although

28. 1 H. Gibb & H. Bowen, *Islamic Society and the West* 30 (1957). The term "Caliph" comes from the Arabic *khalifa* meaning deputy or representative. A. Guillaume, *Islam* 79 (1954). On the development and history of the Caliphate, see T. Arnold, *The Caliphate* (1965).

29. 1 Gibb & Bowen, *supra* note 28, at 27.

30. See *id.* at 28.

31. Arnold, *supra* note 28, at 19-20.

32. *Id.* at 20. Because of Abu Bakr's age, Umar had been the virtual ruler even while his predecessor was alive. *Id.*

33. E. Calverley, *Islam: An Introduction* 38 (1974). As he lay dying, Umar allegedly refused to select his successor. Others suggest, however, that he appointed a body of six electors to choose the next Caliph. Arnold, *supra* note 28, at 21.

34. Calverley, *supra* note 33, at 38.

35. *Id.* at 39, 43. In 676 Mu'awiyah, like Abu Bakr, nominated a successor, but introduced a new element into the process of nomination. Mu'awiyah nominated his son Yazid to be the next

some could argue from these examples that elective leadership was the precedent adopted by Islam,³⁶ it seems to have been honored as much in the breach as in the observance. Thus, in the early period of Islam, election, nomination, and usurpation all seemed to have been accepted as methods of achieving the Caliphate. The legitimacy of a claimant was not judged so much by the manner of his achieving power as by the fact that he had achieved power.

By the end of the eleventh century, the religious institution of the Caliphate had lost power to the temporal institution of the Sultanate.³⁷ Although, at first, Sultans were technically designated by the Caliph, in time even this sham was omitted, the Sultans no longer recognizing the theoretical sovereignty of the Caliph.³⁸ As with the Caliphate before, however, whoever was successful in acquiring the Sultanate was recognized as the legitimate ruler. One Muslim jurist graphically illustrated this principle when he remarked: "The sovereign has a right to govern until another and stronger one shall oust him from power and rule in his stead."³⁹ One modern commentator expressed the point this way: "Muslim society . . . fatalistically disclaimed responsibility for government and failed to establish in the name of the Shari'ah an airtight guarantee of individual and community rights against arbitrary authority."⁴⁰

b. Support for the Existing Ruler

If Islam did not judge the legitimacy of how a ruler acquired power, it did counsel support of that ruler once he had obtained power. In *Surah* 4, verse 59, the Koran says: "Obey Allah, and obey the messenger and those of you who are in authority"⁴¹ Mohammed went one step further when he advised Muslims to "endure patiently" even the yoke of an evil leader.⁴² Centuries later the theologian Ghaz-

Caliph, creating the first family dynasty (The Umayyads) in Islam. *Id.* at 43. See also Arnold, *supra* note 28, at 22-23.

36. Sir Thomas Arnold in his book on the Caliphate suggests that some form of election was involved in the case of each of the first four Caliphs—even in the case of Abu Bakr's appointment of Umar. See Arnold, *supra* note 28, at 21-22.

37. The Legacy of Islam 414-15 (J. Schacht & C. Bosworth eds. 1974) [hereinafter cited as Schacht & Bosworth].

38. See 1 Gibb & Bowen, *supra* note 28, at 31-32. See also Schacht & Bosworth, *supra* note 37, at 412-15.

39. Schacht & Bosworth, *supra* note 37, at 415 (quoting Ibn Jama'a, a *qadi* of Damascus).

40. Nolte, *The Rule of Law in the Arab Middle East*, 48 *Muslim World* 295, 303 (1958).

41. The Meaning of the Glorious Koran 85, *Surah* IV, v. 54 (M. Pickthall trans. 1961) [hereinafter cited as Koran].

42. The remark of the Prophet was reported by Abu Yusuf. See Gibb & Bowen, *supra* note

zali would say: "An evil-doing and barbarous Sultan . . . must be obeyed."⁴³ If Islam counselled submission to authority whether that authority was good or evil, it follows that Islam would reject the right of the community to revolt against that authority. Revolution broke the unity of Islam and therefore had to be avoided at all costs. An early exposition of the *Summi* creed spoke quite clearly to this point:

We uphold the prayer for peace for the Imams of the Muslims and submission to their office, and we maintain the error of those who hold it right to rise against them whensoever there may be apparent in them a falling-away from right. We are opposed to armed rebellion against them and civil war.⁴⁴

"Sixty years of tyranny . . . are better than one hour of civil strife,"⁴⁵ went the Arab maxim. In Islam, subservience to the wishes of the ruler was viewed as a virtue and not as a vice. Thus, in contradistinction to the American model, the Muslim legal model places a heavier emphasis on the autonomy of the political ruler.⁴⁶

2. Constitutional Restraints

As its second constitutive element, the American model places definite limits on the exercise of executive and legislative power by constitutional guarantees. For example, the due process clause of the fifth and fourteenth amendments, the equal protection clause of the fourteenth amendment, and the fifth amendment guarantee that just compensation be paid for property taken for a governmental purpose, all limit the acceptable range of governmental decision-making. In the classical Muslim legal model, there also existed limitations on the power of the ruler.

In the Arab Middle East, Islam is, of course, the dominant religion. The basic text of Islam is the Koran. To a Muslim, the Koran is the immutable word of God and its prescriptions cannot be disobeyed either by the ruler or his subjects. The Koran prescribes rules of

28, at 28. Mohammed also was alleged to have required obedience to the ruler in quite graphic terms. "O men, obey God, even though He sat over you as your ruler a mutilated Abyssinian slave." Arnold, *supra* note 28, at 49. For other *hadith*, or sayings, of the Prophet counseling obedience to rules, see *id.* at 48-50.

43. Anderson & Coulson, *The Moslem Ruler and Contractual Obligations*, 33 N.Y.U.L. Rev. 917, 931 (1958).

44. 1 Gibb & Bowen, *supra* note 28, at 28 n.3.

45. Anderson & Coulson, *supra* note 43, at 931.

46. In speaking of the history of Egypt, one commentator described the importance of the ruler as follows: "Throughout Egypt's history political power and government functioning have been characterized by personality-oriented executive control, whether by a pharaoh, caliph, khedive, king, or president." R. Nyrop, B. Benderly, W. Cover, D. Eglin & R. Kirchner, *Area Handbook for Egypt* 184-85 (3d ed. 1976) [hereinafter cited as *Area Handbook for Egypt*].

conduct for such matters as marriage,⁴⁷ divorce,⁴⁸ inheritance,⁴⁹ the treatment of orphans,⁵⁰ and the punishment of crimes.⁵¹ Similarly, the Koran exhorts Muslims to act justly and honestly and to live up to their contracts.⁵² Because the Koran set forth fundamental and changeless principles, as to matters covered by its text, the Koran acted as a form of constitution, limiting the exercise of the ruler's power. But the Koran was not overly specific on most issues and other legal principles developed to supplement its provisions. The *sunna*, or practice of the prophet, *ijma*, or the consensus of Muslim religious scholars, and *qiyas* or analogical reasoning provided the sources for these supplementary legal rules.⁵³ As one scholar has remarked, these rules of the *Sharia* "generally imposed a restraint upon the ruler through his own piety or through his political prudence during an era when the *qadis* and jurisconsults wielded an enormous popular prestige"⁵⁴ But as has been pointed out above, just as the *Sharia* imposed certain restrictions on the ruler, it also counselled his subjects to tolerate him even when he acted against the tenets of the law. Thus, in the classical Muslim model, there developed what has been termed "a qualified rule of law,"⁵⁵ resulting in a system in which the ruler appears less clearly restricted in the exercise of his authority than in the American model.

But perhaps it is inaccurate to compare the American constitutional model with the classical Muslim model because, during the nineteenth and twentieth centuries, the Middle East has undergone a process of Westernization.⁵⁶ In the process many Middle Eastern nations have adopted Western-styled constitutions which contain precise textual guarantees against arbitrary governmental action. For example, in 1971, Egypt enacted a new constitution.⁵⁷ Freedom of religion and the press were guaranteed.⁵⁸ Every Egyptian was considered to be equal before the

47. See, e.g., Koran, *supra* note 41, at 81-82, *Surah* IV, vv. 22-25 (listing forbidden degrees of marriage).

48. *Id.* at 54, *Surah* II, vv. 230-32. But see the *hadith* of Mohammed: "The thing which is lawful, but disliked by Allah, is divorce." I. Kashmiri, *Prophet of Islam: Muhammad and Some of His Traditions* 91 (1967).

49. Koran, *supra* note 41, at 80, *Surah* IV, vv. 11-12.

50. *Id.* at 79-80, *Surah* IV, vv. 6-10.

51. *Id.* at 100, *Surah* V, v. 38; *id.* at 253, *Surah* XXIV, v. 2.

52. See, e.g., *id.* at 59-62, *Surah* II, vv. 282-86; *id.* at 83, 93, *Surah* IV, v. 33.

53. For a brief discussion of these sources of classical Islamic law, see I. M. Khadduri & H. Liebesny, *Law in the Middle East* 90-97 (1955).

54. Nolte, *supra* note 40, at 303.

55. *Id.*

56. For a brief study of this process of Westernization, see Bonderman, *Modernization and Changing Perceptions of Islamic Law*, 81 Harv. L. Rev. 1169 (1968).

57. For the full text of the Egyptian Constitution, see 26 Middle East J. 55 (1972).

58. *Id.*

law.⁵⁹ Arrest and seizure without court order were outlawed.⁶⁰ More importantly, for the purposes of this Article, article 35 of the 1971 constitution prohibited property nationalization except when dictated by the public interest and then only when compensated.⁶¹ Textually, the Constitution of Egypt is perhaps more libertarian than the Constitution of the United States.

But on closer analysis this process of Westernization, of formally changing the structure of Middle Eastern legal systems to conform to Western models, may have had the unintended effect of making the two models (the American and the Muslim) less, rather than more, similar. As Richard Nolte has pointed out: "By thrusting the Shari'ah far into the background, the influence of secular conceptions from the West has mostly dissolved the qualified rule of law imposed during the centuries of classical Islam. Never fully controlled, the ruler now appears to be fully uncontrolled from a Shari'ah point of view."⁶² Although weakening the traditional legal restraints, Western constitutional norms have not had time to take root, or to replace the older restraints with a new set of legal restraints on the power of the ruler.⁶³ For example, the American Constitution has lasted 195 years. The present Egyptian Constitution has been in effect only since 1971, and the previous constitution of Egypt—the Constitution of 1964—lasted only 7 years.⁶⁴ Although age is not a criterion for fairness or effectiveness, it may indicate that a country has

59. *Id.*

60. *Id.*

61. *Id.* Significantly, however, the Constitution does not qualify the word compensation with any adjective like "just" or the like. For reference to the compensation paid foreign interests during the Nassar expropriations, see Doherty, *Rhetoric and Reality: A Study of Contemporary Official Egyptian Attitudes Toward the International Legal Order*, 62 Am. J. Int'l L. 335, 349 nn.95 & 96 (1968). Egypt seems to maintain that a state may nationalize foreign assets upon payment of adequate compensation. Foreign investments under Egypt's new open-door policy are immune from nationalization. Law No. 43 of 1974 Concerning The Investment of Arab and Foreign Funds and the Free Zones art. 7 (Egypt), as amended by Law No. 32 of 1977 (Egypt) [hereinafter cited as Law No. 43] (copy on file with the *Fordham Law Review*). Assets of such projects can be confiscated only pursuant to judicial procedures. *Id.* Law No. 43, however, makes no reference to compensation after confiscation. Prior investment laws did make such references. See Salacuse, *Egypt's New Law on Foreign Investment: The Framework for Economic Openness*, 9 Int'l Law. 647, 653 (1975).

62. Nolte, *supra* note 40, at 307. See also N. Coulson, *Conflicts and Tensions in Islamic Jurisprudence* 69 (1969).

63. Nolte, *supra* note 40, at 307.

64. Area Handbook for Egypt, *supra* note 46, at 166. The first written Egyptian constitution was promulgated in 1923 but was suspended during 1928 and 1929. *Id.* at 164. From October of 1930 to December of 1935, a substitute constitution was in effect. The Constitution of 1923 was fully abrogated in 1952 and a new constitution was promulgated in 1953. *Id.* at 164-65. In 1959, because of the merger of Egypt and Syria into the United Arab Republic, yet another constitution was adopted. When that union failed, a National Charter was promulgated in Egypt in 1962, which lasted for two years. *Id.* at 166.

come to view its constitution more as a fundamental and rarely changed document than as an ordinary piece of legislation. Thus, Westernization has, on the one hand, weakened the traditional restraints on the ruler's power and, on the other, has as yet failed to substitute a new set of restraints in their place. The effect of this process can only be a net gain for the ruler. Thus, the ruler, already stronger in the Muslim legal model than in the American model, may have become stronger still due to the process of Westernization, with its concomitant weakening of traditional values.

3. The Judiciary

The final element of the American model to be discussed is an independent judiciary with the power of judicial review. Although the system of checks and balances provides the other branches of government with some control over the American judiciary, by and large the judiciary is free of direct political control.⁶⁵ More importantly for this discussion, however, the courts have asserted the right to review the acts of the other branches of government—to test their actions against the guarantees provided in the Constitution. Thus, along with the Constitution, the American judiciary provides a brake on capricious governmental action.

On the question of an independent judiciary with the power of judicial review, the Islamic model differs in significant respects from the American model. The first important difference, however, is perhaps cultural rather than legal. Every society must provide a mechanism for dispute resolution. In the United States that function is performed primarily by the courts. In the Arab tradition, tribal or village mediation has for centuries been the prime method for settling disputes.⁶⁶ This process of mediation has as its primary purpose the reconciliation of the parties, not the determination of who is right or wrong or who has the superior claim.⁶⁷ While the verdict of a court formally ends the dispute in the eyes of society, it often fails to resolve the hostility between the disputants. As a consequence, research has disclosed that in the Middle East there is "resistance to the use of courts."⁶⁸ Thus, culturally, the courts in the Middle East seem to provide a less important mechanism for dispute resolution than in the United States. Traditional forms of mediation or conciliation are preferred.

65. The United States Constitution may, however, permit some degree of congressional control over the appellate jurisdiction of the United States Supreme Court. U.S. Const. art. III, § 2; see *Ex parte McCordle*, 74 U.S. 506 (1869). But see *Glidden Co. v. Zdanok*, 370 U.S. 530, 605 n.11 (1962) (Douglas, J., dissenting).

66. Patai, *supra* note 27, at 228.

67. *Id.* at 231.

68. *Id.*

Any discussion of the second important difference between the American and Muslim judicial models requires a general understanding of the traditions out of which the Muslim system grew. To focus the discussion, the legal traditions which have molded the contemporary Egyptian legal system will be briefly considered. The British, the French, and the traditional Muslim legal traditions have all contributed strongly to the philosophy and structure of the contemporary Egyptian judiciary. The three traditions will be treated in historical order and the Islamic tradition, being the oldest, will be considered first.⁶⁹

a. The Islamic Tradition

In classical Islamic jurisprudence, the *qadi*, or Islamic judge, was not independent from the one who appointed him.⁷⁰ Thus, since the Caliph, and later the Sultan, was the supreme power in the Muslim state, all *qadis* ultimately owed their position to the ruler through a complex process of subdelegation of that supreme power.⁷¹ In the Ottoman judicial system for instance, the ruler appointed two chief judges or *qadi askers*—one as chief judge of *Rumelia* (Europe) and one as chief judge of *Anatolia* (Asia).⁷² Below the chief judges were varying grades and degrees of judges. In the European half of the judiciary there were, for example, nine such grades.⁷³ Each one of these inferior judges was technically appointed by the Sultan (usually for a price) and served at his pleasure.⁷⁴

Appointment as a *qadi* brought with it jurisdiction to hear cases. But whoever appointed the *qadi* could initially restrict that jurisdiction, either as to venue or as to the class of case to be heard.⁷⁵ Similarly, once given, jurisdiction could later be suspended or curtailed. Collegial decision-making was prohibited in Islam—the judge could consult a *mufti* (or legal scholar), but ultimately the judge alone was accountable to the one who appointed him for the correctness of the decision.⁷⁶ Putting these factors together, one can sense why, in the

69. The Mixed Courts of Egypt might be considered a fourth influence. Since the Mixed Courts were basically influenced by French models, they have not been separately considered. Because they were strongly supported by the capitulatory powers in Egypt, they did maintain an independence from the government. On the subject of the Mixed Courts, see J. Brinton, *The Mixed Courts of Egypt* (1968).

70. Khadduri & Liebesny, *supra* note 53, at 236.

71. *Id.* at 236-37.

72. W. Vucinich, *The Ottoman Empire: Its Record and Legacy* 38 (1965).

73. *Id.*

74. Most often the ruler would appoint the more important *qadis*, who would in turn subdelegate their jurisdictional authority to others. Khadduri & Liebesny, *supra* note 53, at 237.

75. *Id.* at 239.

76. *Id.* at 241-45.

early Muslim legal model, there was a "complete lack of separation between the judicial and executive powers."⁷⁷ Although the ruler could not tamper with the substance of the *Sharia*—since he too was bound by it—by the simple device of restricting the competence of the *qadis* with respect to venue or subject matter, the ruler could effectively achieve his goals without significant judicial interference.⁷⁸ Perhaps the most sweeping statement of the supremacy of the political ruler over the *qadi* occurred in the Ottoman Empire of the sixteenth century. The legal scholar Abul Su'ad broadly reformulated the principle that the *qadi* was required to follow the Sultan's instructions in carrying out the *Sharia*.⁷⁹ Although at various times in Islamic history the *qadi* did achieve some degree of autonomy from the ruler,⁸⁰ generally speaking, the power of the ruler to suspend the competence of the *qadi* to hear certain classes of cases provided an effective veto over judicial intervention in the political arena.⁸¹

b. The British Tradition

If classical Islamic legal theory effectively made the *qadi* subservient to the political branches of government, the arrival of British jurisprudence in Egypt did little to change this.

Although Egypt was nominally a part of the Ottoman Empire, Britain exercised a proconsular influence in the country after the year 1882.⁸² Unlike his American counterpart, however, the British judge of the nineteenth century did not consider it his function to oppose the will of the ruler—which in the British system of government was Parliament. But that had not always been the case. During the seventeenth century in the famous *Bonham's Case*, Lord Coke had said:

And it appears in our books that in many cases the common law will controul Acts of Parliament and sometimes adjudge them to be utterly void: for when an Act of Parliament is against common right and reason, or repugnant, or impossible to be performed, the common law will controul it, and adjudge such act to be void . . .⁸³

But the doctrine of *Bonham's Case* was gradually abandoned as Parliament grew in power after the Glorious Revolution of 1688.⁸⁴ Although

77. *Id.* at 239.

78. This device of restricting the competence of the Islamic courts has been used in the twentieth century to "modernize" Islamic law. See N. Coulson, *A History of Islamic Law* 172-81 (1964); N. Coulson, *Conflicts and Tensions in Islamic Jurisprudence* 73-75 (1969).

79. J. Schacht, *An Introduction to Islamic Law* 90 (1964).

80. Khadduri & Liebesny, *supra* note 53, at 240.

81. See note 78 *supra*.

82. 1 *The Cambridge History of Islam* 388 (P. Holt, A. Lambton & B. Lewis eds. 1970).

83. *Bonham's Case*, 77 Eng. Rep. 646, 652, 8 Co. Rep. 114b, 118a (C.P. 1610) (footnote omitted).

84. T. Plucknett, *A Concise History of the Common Law* 337 (1956).

clearly eroded by earlier eighteenth century decisions,⁸⁵ it was not until 1871 that the rule of *Bonham's Case* was categorically rejected. In *Lee v. Bude & Torrington Junction Ry.*, the court observed that

as to these Acts of Parliament . . . they are the law of this land; and we do not sit here as a court of appeal from Parliament We sit here as servants of the Queen and the legislature. Are we to act as regents over what is done by Parliament with the consent of the Queen, lords and commons? I deny that any such authority exists.⁸⁶

Thus, when the British occupied Egypt in 1882, English judges had come to view their function as nothing more than servants of the legislature.⁸⁷

c. The French Tradition

Although aware of the British tradition both through schooling and through the large numbers of British judges on the Mixed Courts of Egypt,⁸⁸ it was still the French, not the British, tradition which was the more important European influence on the development of Egypt's legal institutions. As one commentator remarked: "[A]fter forty years of the British Occupation, British officials were administering French law in Arabic, teaching French law in English, and arguing French law in French"⁸⁹

The *Code Napoléon* and post-revolutionary French judicial notions became models for many institutions and aspects of Egyptian law.⁹⁰ Prior to the French Revolution, if a French *parlement* (court) disapproved of a royal ordinance, it could refuse to put the ordinance into effect.⁹¹ The King could overcome judicial resistance only by appearing personally in court.⁹² After the Revolution, however, judicial independence was severely curtailed. Since law making was viewed as

85. Plucknett, *Bonham's Case and Judicial Review*, 40 Harv. L. Rev. 30, 58-59 (1926).

86. 6 C.P. 576, 582 (1871).

87. Parliament, to use a picturesque phrase, "could do anything except make a man a woman." Plucknett, *supra* note 84, at 337. Paradoxically, the principle of parliamentary supremacy which resulted in the removal of judicial control over the validity of legislation in England, had the opposite result in the American colonies. M. Cappelletti, *Judicial Review in the Contemporary World* 40 (1971).

88. From 1875 until 1949, there were 9 judges from Great Britain on the Court of Appeals and 23 in the District Courts. Only France had a larger number of judges in the Mixed Courts. Brinton, *supra* note 69, at 231.

89. *Id.* at 87 n.4.

90. *Id.* at 86-87. See also B. Schwartz, *The Code Napoléon and the Common-Law World* 101-02 (1956).

91. P. Herzog, *Civil Procedure in France* 44-45 (1967). The *parlements* developed from the *Parlement* of Paris—a special section of the King's Council which began to sit especially to handle judicial business. In time, local *parlements* were established throughout the country. *Id.* at 42-44.

92. *Id.* at 45.

exclusively the prerogative of the popular assemblies, French courts were forbidden to interfere with the legislative will.⁹³ There was a "rigid separation of powers in which the judge, the passive and 'inanimate' *bouche de la loi*, performed the sole task of applying the letter of the law to individual cases—a task conceived as purely mechanical and in no way creative."⁹⁴ Thus, judicial review in the American sense of the word never developed in post-revolutionary France, the courts being viewed as totally subservient to the legislature.

French judicial philosophy has not changed to the present day. Under the 1958 Constitution, the judiciary is, in effect, an appendage of the executive branch of government.⁹⁵ In fact, the French Constitution does not even mention the judicial branch, speaking only of judicial authority.⁹⁶ Carrying on the post-revolutionary tradition, the Constitution does not give the French courts the power to review the constitutionality of legislation. Constitutional review is made the function of a newly established *Conseil Constitutionnel*, a body composed of nine members, three appointed by the executive and six by the legislature.⁹⁷ For various reasons, however, the legislative review provided by the *Conseil* is markedly different from what has traditionally been understood by judicial review.⁹⁸ Thus, the French legal tradition, like the British before it, did little to alter the traditional Islamic view that the *qadi* or judge had no right to review the decrees of the ruler.⁹⁹

93. *Id.* at 47.

94. Cappelletti, *supra* note 87, at 35.

95. Herzog, *supra* note 91, at 39.

96. *Id.*

97. *Id.* at 118. The *Conseil* is the first body in French history which has had the power to declare acts of the legislature unconstitutional. *Id.* at 25.

98. Cappelletti, *supra* note 87, at 4-6.

99. One commentator has argued that because of their professional training, the European judges never developed the policy-oriented skills necessary for judicial review. *Id.* at 62-63.

The Mixed Courts of Egypt, however, did develop a form of constitutional review. Any decree violating the capitulations would not be enforced in the Mixed Courts. Brinton, *supra* note 69, at 131. As a practical matter, however, a law, to be applicable to foreigners, had to be approved by one of the two legislative branches of the Mixed Courts or by the capitulatory powers themselves. Thus, it would be difficult to argue that a law violated the capitulations if the capitulatory powers had already consented to it. *See id.* at 131-32.

There are hopeful signs, however, that the structure of the Egyptian judiciary may undergo a significant transformation in the future. The 1971 Constitution of Egypt provides the framework for a judiciary similar in many respects to the American model. Articles 165 and 166 state that the judges and the judicial authority are independent. Articles 174 through 178 create a Supreme Constitutional Court with power to review legislative acts. Egyptian Const. arts. 165-66, 174-78, reprinted in 26 Middle East J. 55, 67 (1972). The Supreme Constitutional Court must be watched to see if it effectively exercises judicial review. For an argument that the Egyptian courts have a tradition of independence, objectivity and fairness, see Goekjian, *Specific Problems and Unique*

If the foregoing analysis is accepted, there appear to be important differences between the American legal model and the Muslim legal model. Because of its emphasis on the power of the ruler on the one hand, and the relative weakness of constitutional and judicial restraints on the other, the Middle East legal model has fewer inherent checks against arbitrary governmental action than does the American model.¹⁰⁰ If this comparative analysis were applied systematically to every country in the world, one would undoubtedly find that this increased potential for arbitrary government action exists in many legal systems. It is now necessary to relate legal models with this greater potential for arbitrary governmental action to the question of foreign corporate payments.

B. Questionable Payments in Different Legal System Models

1. The Corrupt Motive

The legislation recently enacted by Congress criminalizes payments made to foreign officials which are "corruptly" made.¹⁰¹ The term "corruptly" implies a high degree of criminal purpose¹⁰²—a purpose to influence the foreign official to select the approach most favorable to the payor from among the range of alternative approaches available to the official. For the sake of argument, assume that on any given question a foreign government official could make four different decisions—decision A, B, C, or D. Assume further that decision A would be totally

Aspects of Doing Business in Egypt, reprinted in *Current Legal Aspects of Doing Business in the Middle East—Saudi Arabia, Egypt and Iran* 179, 187 (1977), and Habachy, *Doing Business in Egypt—Comments*, reprinted in *Current Legal Aspects of Doing Business in the Middle East—Saudi Arabia, Egypt and Iran* 190, 191-92 (1977).

100. It must again be emphasized, however, that even within the overall Middle East model, there will be significant variations from country to country.

In his dissent in *In re Griffiths*, 413 U.S. 717 (1973), Mr. Justice Rehnquist suggested that it was not irrational to think that differences in the political and social structure of a foreign country could adversely affect an alien's abilities to work within the American political and legal model. "It is not irrational to assume that aliens as a class are not familiar with how we as individuals treat others and how we expect 'government' to treat us. An alien who grew up in a country in which political mores do not reject bribery or self-dealing to the same extent that our culture does; in which an imperious bureaucracy historically adopted a complacent or contemptuous attitude toward those it was supposed to serve; in which fewer if any checks existed on administrative abuses; in which 'low-level' civil servants serve at the will of their superiors—could rationally be thought not to be able to deal with the public and with citizen civil servants with the same rapport [as] one familiar with our political and social mores . . ." *Id.* at 662 (Rehnquist, J. dissenting). It has been alleged that the judges at one recent trial in Pakistan were "very submissive and obliging to the military Government." *N.Y. Times*, Mar. 20, 1978, § A, at 3, col. 4; see *id.* Mar. 25, 1978, at 2, col. 3.

101. See note 13 *supra*.

102. See note 24 *supra*.

arbitrary—a decision based on no other ground than the whim of the decisionmaker. Decisions *B*, *C*, and *D* on the other hand, are all reasonable in terms of different governmental policy concerns. In the American model, the courts and constitution would prohibit an official from making decision *A*, but would not restrict his power of choice among decisions *B*, *C*, or *D*. Thus, a payment made in the American system would usually be “corruptly” made since its purpose would be to influence the decisionmaker in his choice between alternatives *B*, *C*, or *D*—a choice which should be based on policy concerns rather than on personal greed. But, in a legal system where there are fewer restraints imposed on the decisionmaker—restraints which would prevent him from also choosing alternative *A*—is it as clear that a payment made would reach the high degree of culpability necessary before a payment can be found to be “corruptly” made?

Assume that an American company has an existing investment in a certain South American country whose ruler is a dictator. The company learns that the ruler of the country wishes to be paid money in return for the continued goodwill of the government toward the company. The failure to pay would result in harassment of the company; for example, the arbitrary revocation of discretionary work permits for foreign employees or the refusal to permit the company to bid on future contracts. If the payment is made, its purpose will have been to influence the acts of the dictator; that is, to influence him not to act arbitrarily. If one of the reasons for making a payment is to hedge against possible future arbitrary action—action which cannot be effectively resisted in a foreign court—has the payment been corruptly made? The legislative history of the Foreign Corrupt Practices Act makes it clear that under these conditions the payment would be considered “corruptly” made because the corporation made a conscious decision to bribe.¹⁰³ Only payments made in true extortion situations, a payment, for example, to an official to keep an oil rig from being dynamited, would be considered not corruptly made—presumably because a payment made under extreme duress cannot be said to be corrupt.¹⁰⁴ But, in legal systems where there is a greater potential for arbitrary government action, there would seem to be an inherent coercive element present whenever a payment is requested, whether implicitly or explicitly. Depending on the circumstances, this coercive element might be sufficiently strong to negate the high degree of culpability needed for a corrupt motive.¹⁰⁵

103. Senate Report, *supra* note 17, at 10-11.

104. *Id.* at 11.

105. The author does not mean to suggest that all payments made in these legal systems are ipso facto “non-corrupt.” Corrupt motives may be the prime reason for these payments even in a legal system with a greater potential for arbitrary action.

2. Compensating Mechanisms

If structural differences among legal systems may directly affect the prosecutor's task of proving a corrupt motive under American law, structural differences may create a wholly different set of problems for the legislator. In a legal system where a foreign government is less restricted by court and constitution, an American legislator may well ask whether compensating mechanisms exist by which an American company, operating in a different legal system, can achieve protection against arbitrary government action comparable to that afforded in the American system. Several possible compensating mechanisms must be considered.

a. Insurance

The Overseas Private Investment Corporation (OPIC) was created in 1969¹⁰⁶ to "mobilize and facilitate the participation of United States private capital and skills in the economic and social progress of less developed friendly countries and areas"¹⁰⁷ OPIC provides a program which insures against: a) the inability of an American investor to convert into dollars local currency received as earnings or profits or return of its original investment;¹⁰⁸ b) loss of its investment due to expropriation or confiscation;¹⁰⁹ or c) loss of its investment due to war, revolution or insurrection.¹¹⁰ Since an American corporation is eligible for any or all of these programs—no matter what the form of its foreign investment might be—the existence of this insurance program might provide a sufficient degree of property protection to obviate the need for payments to government officials. The president of OPIC made this point quite forcefully in testimony before the House Committee on International Relations. OPIC insurance, he argued,

will protect the U.S. investor who is the victim of extortion by a Government official who threatens expropriation or some other sanction against him if he fails to make the payment. It is a protection because the insured investor in that case knows that he can call on OPIC and our insurance in the event that action is taken against him.¹¹¹

Realistically, however, the existence of OPIC insurance has little practical impact on the question of whether or not to accede to a payment request. First of all, OPIC does not provide complete insurance coverage. OPIC usually insures only 90% of the investment and in some cases much

106. 83 Stat. 809 (1969) (codified at 22 U.S.C. §§ 2191-2199 (1970)).

107. 22 U.S.C. § 2191 (1970).

108. *Id.* § 2194(a)(1)(A).

109. *Id.* § 2194(a)(1)(B).

110. *Id.* § 2194(a)(1)(C).

111. *Hearing and Markup Sessions of the House Comm. on International Relations*, 94th Cong. 2d Sess. 5 (1976) [hereinafter cited as *House Committee Hearings*].

less.¹¹² Second, OPIC will only insure investments in less developed friendly countries¹¹³ which have signed bilateral agreements with the United States recognizing the United States' right of subrogation for any claims paid by OPIC.¹¹⁴ In the Middle East, such agreements exist with Egypt,¹¹⁵ Saudi Arabia,¹¹⁶ Jordan,¹¹⁷ Syria,¹¹⁸ the Sudan,¹¹⁹ Yemen,¹²⁰ Morocco,¹²¹ and Tunisia¹²² but not with Algeria, Libya, Iraq, or Lebanon. Even in countries where OPIC insurance is available, the proposed project or investment requires two approvals—the approval of the host country and the approval of OPIC.¹²³ Third, OPIC's approval is not based solely on the economic strength or weakness of the project. OPIC is required to scrutinize the project to see if the investment will have a substantial negative effect on American employment or on the United States balance of payments.¹²⁴ Similarly, OPIC must deny insurance coverage to a project which is "likely to cause . . . [the] investor . . . significantly to reduce the number of his employees in the United States [because] he is replacing his United States production with production from such investment which involves substantially the same product for substantially the same market as his United States production . . ."¹²⁵ In certain cases, these requirements could be significant limitations on the

112. OPIC's statute requires the insured company to provide for at least ten percent of the insurance. 22 U.S.C. § 2197(f) (Supp. IV 1974). For large investments, OPIC will limit expropriation coverage to seventy-five percent and often as low as fifty percent. Overseas Private Investment Corporation, Investment Insurance Handbook 8-9 (1975) [hereinafter cited as Investment Insurance Handbook]; see 22 U.S.C. § 2194(a)(4)(A) (Supp. IV 1974).

113. 22 U.S.C. § 2191 (1970).

114. See *id.* § 2197(a).

115. [1963] 14 U.S.T. 945, T.I.A.S. No. 5383, 479 U.N.T.S. 207.

116. [1975] 26 U.S.T. 459, T.I.A.S. No. 8045.

117. [1956] 7 U.S.T. 2829, T.I.A.S. No. 3663. Jordan's agreement is typical of the others. The United States agrees not to guarantee any project by American nationals in Jordan unless the Jordanian Government first approves the project. *Id.* § 2. Also, if the United States Government pays any money under the guaranty, any right, title, or interest in the project passes to the United States Government and it becomes subrogated to any claim or cause of action. *Id.* § 3(a).

118. [1977] — U.S.T. —, T.I.A.S. No. 8707.

119. [1959] 10 U.S.T. 408, T.I.A.S. No. 4201, 342 U.N.T.S. 13.

120. [1972] 24 U.S.T. 845, T.I.A.S. No. 7586.

121. [1961] 12 U.S.T. 386, T.I.A.S. No. 4728, 406 U.N.T.S. 249.

122. [1959] 10 U.S.T. 858, T.I.A.S. No. 4224, 344 U.N.T.S. 179, *amended by* [1963] 14 U.S.T. 385, T.I.A.S. No. 5329, 474 U.N.T.S. 344. The agreements with Morocco, Tunisia, and the Sudan were all made under the Mutual Security Act of 1954. 22 U.S.C. § 1933(b)(4) (repealed 75 Stat. 460 (1961)). Even though the Act has been repealed, all guarantees made under it are still valid. 22 U.S.C. § 2197(c) (1970).

123. OPIC's approval is required by statute. 22 U.S.C. § 2191 (1970). The approval of the host government is required by the agreement between the United States and the respective government.

124. *Id.* § 2191(i) (Supp. IV 1974).

125. *Id.* § 2191(m)(1).

availability of OPIC insurance. Fourth, there is at least some concern expressed that OPIC, like the Securities and Exchange Commission (S.E.C.), may be pressured into policing the corporate practices of its clients.¹²⁶ The procuring of OPIC insurance would provide the United States Government with a sufficient handle to inquire into many other sensitive areas of a company's foreign business practices.¹²⁷ Fifth, allegations have been made that OPIC often assumes a skeptical stance—even against the grossest sort of foreign government action—and resists the payment of large claims.¹²⁸ Such a policy stance, of course, seriously undercuts OPIC's usefulness. Sixth, OPIC insurance does not protect the on-going business profits of the investor while payments made to foreign officials arguably do. Once a company is expropriated, or some foreign government sanction is imposed on it, future profits are lost and not compensated for by OPIC insurance. Since companies are in business to make a profit, the questionable payment, rather than OPIC insurance, may better protect this ongoing profitability of the company. Seventh, although OPIC insures against expropriatory action, the definition of that term excludes proper regulatory or revenue actions by the foreign government.¹²⁹ Because government harassment just short of expropriatory action can take so many forms, it may be difficult for a corporation to prove that certain conduct is, in fact, expropriatory rather than harassment or proper regulatory action. Eighth, in the standard insurance contract used by OPIC, the investor must warrant that his project is in conformity with all applicable laws of the project country

126. OPIC's president has testified that OPIC should not become a regulatory agency because of its small staff and the congressional directive to make OPIC a largely private business. *House Committee Hearings*, *supra* note 111, at 15. OPIC's vice-president has expressed a more general concern. "I have my doubts whether we in this country can police the morality of the world Also I would be very reluctant to get into that sort of situation because how would one determine whether or not a bribe had been extorted from a U.S. investor? . . . Such a mechanism could create very serious foreign relations problems by forcing the U.S. Government to take actions which could be easily regarded as outrageous interference in the governmental affairs of a foreign country." *The Activities of American Multinational Corporations Abroad, Hearings before the Subcomm. on International Economic Policy of the Comm. on International Relations, House of Representatives*, 94th Cong., 1st Sess. 17 (1975) [hereinafter cited as *House Subcommittee Hearings*].

127. For several such sensitive practices, see Report to the Shareholders of the General Tire & Rubber Company, July 19, 1977, at 5-6.

128. In an effort to encourage investors and foreign governments to avoid nationalization by resolving their own disputes, OPIC, in 1971, adopted a policy of settling claims instead of just paying them and then asking Congress for more money. Gilbert, *Expropriations and the Overseas Private Investment Corporation*, 9 Law & Pol'y Int'l Bus. 515, 517 (1977). In cases where negotiations fail, OPIC has been accused of trying to reduce its payment on the claim. *Id.* at 535.

129. *Investment Insurance Handbook*, *supra* note 112, at 10. This definition of expropriation is not in OPIC's statute, but it is part of the standard OPIC contract. *Id.*

that can be ascertained by reasonable investigation.¹³⁰ The contract excludes losses resulting from provocation or instigation on the part of the investor or from the lawful prosecution of illegal acts.¹³¹ A comparative legal systems analysis shows how confusing these contract provisions really are. American companies may argue that quite often the statutes of a country are unclear or that the statutes say one thing but the practice says another. Is one in conformity with applicable laws if one follows the unwritten as opposed to the written law of a country? Furthermore, what does provocation or instigation on the part of the investor mean and from what perspective are these questions to be judged? A corporate payment might be considered a provocative act in the United States but totally acceptable in a differently structured legal system. For these reasons, OPIC insurance may not be a realistic compensating mechanism by which an American company can achieve protection against arbitrary government action.

b. Arbitration

Arbitration may, however, provide a more effective compensating mechanism to curtail arbitrary foreign government action. For example, in Egypt, under article 8 of Law No. 43 of 1974,¹³² an American company can provide in advance for investment disputes to be settled either by private arbitration mechanisms or within the framework of any existing bilateral agreement between the countries or within the framework of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States.¹³³ With any of

130. *House Subcommittee Hearings*, *supra* note 126, at 7.

131. *Id.* at 7-8.

132. Law No. 43, *supra* note 61, art. 8. For a detailed discussion of this statute, see McLaughlin, *Infatih in Egypt: An Appraisal of Egypt's Open Door Policy for Foreign Investment*, 46 *Fordham L. Rev.* 885 (1978).

133. Under this last mentioned convention, the International Centre for Settlement of Investment Disputes makes provision for the creation of a Special Arbitral Tribunal as a mechanism for the settlement of international investment disputes. [1965] 17 *U.S.T.* 1270, T.I.A.S. No. 6090, 575 *U.N.T.S.* 159, ch. IV, § 2, art. 37(1). The Tribunal consists of any uneven number of arbitrators, but if the opposing parties cannot agree on a number, each side can appoint one arbitrator and a third will be appointed by agreement of the parties. *Id.*, ch. IV, § 2, art. 37(2)(b). There are problems with the effectiveness of this procedure, however. First, the International Centre for Settlement of Investment Disputes has jurisdiction over a matter only if both parties agree in writing to submit their dispute to the Centre. *Id.*, ch. II, art. 25(1). Either side can thus block resort to this form of arbitration. Second, even if both sides do agree to arbitration, the final award must be enforced in a court designated by the state within which execution is sought. *Id.*, ch. IV, § 6, art. 54(3). Therefore, in a legal system such as the Middle East, the arbitration procedure does not eliminate the problem of a non-independent judiciary.

In addition to the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, there are two separate bilateral agreements between Egypt and the United States which establish a framework for other forms of arbitration. First, there is a general

these forms of arbitration, however, unless there is voluntary compliance by the government, any arbitration decree must ultimately be enforced in the courts of the foreign country. In a legal model where the judiciary is less independent of the political branches of government than in the American model, pressure may be exerted to render a judgment favorable to the government.¹³⁴ Thus arbitration may not be viewed as a sufficient compensating mechanism because its effectiveness rests on the voluntary compliance of the foreign government—the very thing that a compensating mechanism seeks to avoid.

c. The Local Agent

The local agent may represent a third form of compensating mechanism against arbitrary government action. In most foreign countries, the use of a local agent makes good business sense. In many areas of the world, a Westerner is often viewed with inherent mistrust. Since the agent is a national of the country, he can deal with his fellow countrymen in their own language and with an understanding of the rituals and customs of the local business practice. In addition, the agent chosen will undoubtedly have substantial influence in the country: through either friendship, family or business ties, or perhaps even through past government affiliation. The wisdom of using local agents is supported by the practices of American companies. Lockheed, for example, reported that between 1970 and 1975, it paid more than 150 consultants in fifty foreign countries approximately 165 million dollars in fees.¹³⁵

In the Middle East legal model, where the ruler is virtually supreme on the one hand and there exists a long history of extra-judicial mediation on the other,¹³⁶ the use of local agents would seem to be particularly beneficial. The local agent through his influence can reconcile the company and the government if any dispute arises. Although the laws of several Middle Eastern countries require the

arbitration agreement between Egypt and the United States which provides for submission of a dispute to some competent tribunal such as the Permanent Court of Arbitration at The Hague. 11 Bevens 1325, 47 Stat. 2130, T.S. No. 850, 142 L.N.T.S. 323 (1932). This agreement, however, does not apply to disputes within the domestic jurisdiction of either country. *Id.* art. II(a). The second bilateral United States-Egyptian agreement on arbitration is contained in a provision in the Investment Guaranties Treaty between the two countries. [1963] 14 U.S.T. 945, T.I.A.S. No. 5383, 479 U.N.T.S. 207. This provision provides for the negotiation of any dispute and, if that fails, for "binding" arbitration by a three-member panel.

134. See, e.g., N.Y. Times, Mar. 20, 1978, § A, at 3, col. 4; *id.*, Mar. 25, 1978, at 2, col. 3.

135. Report of the Special Review Committee of the Board of Directors, Lockheed Aircraft Corporation, May 16, 1977, at 29.

136. See Patai, *supra* note 27, at 228.

hiring of local agents,¹³⁷ on further analysis, the use of a local agent does not appear to be a sufficient compensating mechanism for the absence of strong constitutional or judicial protections against arbitrary government action. The agent, although technically representing the foreign company, must in the end also serve the host government. His usefulness as an agent depends upon his governmental connections. If he antagonizes the government in representing his principal, he will lose his influence and therefore also his future effectiveness as an agent. Thus, from the standpoint of the foreign principal, it must be realized that the agent cannot risk a rupture with the government in settling a dispute. The agent will ultimately have to bow to government decisions without strongly opposing them.

d. The Questionable Payment

If neither insurance, arbitration nor the local agent are adequate compensating mechanisms for the lack of a strong judiciary and constitutional guarantees in some legal systems, could the questionable payment serve this function?¹³⁸ If a hypothetical legal system provides

137. Kuwait, for example, requires the hiring of local agents before foreign companies may do business in the country. *Legal Aspects of Doing Business with Egypt, Iran, Saudi Arabia, and the Gulf States* 273 (1975). If the agent is to be a corporation, Law No. 36 of 1964 (Kuwait) requires at least fifty-one percent Kuwaiti ownership of such a company or firm operating as an agent in the country. *An Introduction to Business Law in the Middle East* 80 (B. Russell ed. 1975). On Iraqi law, *see id.* at 83. Iraq, by Law No. 208 of 1969 (Iraq), allows nationals of other Arab countries, as well as Iraqis, to work as agents in Iraq, *id.* at 80, 83. In Egypt, sales agents for foreign sellers must be either Egyptian nationals or an Egyptian company. *See Current Legal Aspects of Doing Business in the Middle East—Saudi Arabia, Egypt and Iran* 195 (W. Wickersham & B. Fishburne eds. 1977); *Legal Aspects of Doing Business with Egypt, Iran, Saudi Arabia and the Gulf States* 259 (1975). Certain Middle Eastern governments have recently taken steps to deemphasize the importance of local agents. Iran, for example, forbids the payment of an agent's fee to be included in the price of any American military equipment sold to the country. "Notwithstanding any other provision of this contract, any direct or indirect costs of agent's fees/commissions for contractor sales agents involved in FMS [Foreign Military Sales] to the Government of Iran shall be considered as an unallowable item of cost under this contract." Defense Procurement Circular #117, Nov. 23, 1973, *quoted in House Subcommittee Hearings*, *supra* note 126, at 102. Iran also requires affidavits from companies selling to the government which state that no fees were paid to secure the contract. *Legal Aspects of Doing Business with Egypt, Iran, Saudi Arabia, and the Gulf States* 351, app. II (1975).

138. Quite often the local agent has been used as a conduit for the questionable payment. By using the agent as the conduit for these payments, a company not only insulates itself from having to make the payment directly but also can assure itself that the payment will reach the appropriate person in the appropriate manner.

Local agents are paid by commission, usually expressed in terms of "points," *i.e.*, a percentage of sales. Although the points may vary, the fee can be quite substantial, permitting an agent to keep a certain amount for himself, yet still have enough left over to buy continued future goodwill for the company. An agent's percentage may be anywhere between the usual four to six percent and the twenty-five percent obtained on smaller sales. The French and British are reportedly

absolutely no restraints on the whims of the ruler, then obviously the only protection offered within that system is the voluntary goodwill of the ruler. If fair treatment by the ruler is either implicitly or explicitly conditioned on payments being made, then the payment would appear to compensate for the lack of any other method of assuring fair treatment. (Again it must be emphasized that this does not mean that taking advantage of the compensating mechanism would necessarily make the payment moral.) But no legal system is as extreme as the hypothetical posited above. In each country, the court system will be more or less independent of the government, or constitutional protections will be more or less guaranteed. Even in the American model, extreme circumstances have seen the dilution of constitutional guarantees.¹³⁹ This very variety poses the dilemma faced by the American legislator in determining whether to criminalize questionable payments. Criminalization may be justified in countries where the legal model is similar to that of the United States, but criminalization becomes progressively less justifiable as a country's legal model has an increasing potential for arbitrary action. Before criminalizing the making of these payments everywhere and under all circumstances, the legislator must be assured that an acceptable degree of protection against arbitrary action exists for American companies in the structure of all other foreign legal systems or through other available compensating mechanisms. Because this is an almost impossible task, it would seem to have been more prudent for Congress to have refrained from criminalizing the making of these payments—at least from the perspective of this comparative legal systems analysis.

Before concluding Part II of this Article, however, two comparative legal systems arguments supporting criminalization should be answered. First, it could be argued in opposition to the conclusion just set forth that Congress should criminalize payments wherever made

masters in dealing through agents. An agent for a European company had, at one time during negotiations, twenty-one points (twenty-one percent) on a \$200 million contract. *House Subcommittee Hearings*, *supra* note 126, at 102.

The position of local agent for foreign companies is obviously quite lucrative. In the past twenty years, the principal shareholder of Triad Financial Establishment—a company which represents many American interests in Saudi Arabia—has made a personal fortune of one hundred million dollars. In addition, Triad itself—with business ventures “ranging from meat packing in Brazil to a multi-million dollar agricultural scheme in the Sudan”—is estimated to have assets of four hundred million dollars. *Saudi Arabia's Super Salesman—Catching U'p with Rockefeller*, *Point*, July 4, 1977, at 24. In one Middle Eastern deal, a French firm made forty million dollars on a contract worth two to three hundred million dollars. *See House Subcommittee Hearings*, *supra* note 126, at 102.

139. *See, e.g.*, the post-World War I free speech cases of *Schenck v. United States*, 249 U.S. 47 (1919); *Debs v. United States*, 249 U.S. 211 (1919); *Abrams v. United States*, 250 U.S. 616 (1919).

and, in those situations where, due to the increased potential for arbitrary action, companies are explicitly or implicitly coerced into making payments, allow the coercion to be introduced as exculpatory evidence on the question of corrupt motive. Although seemingly an appealing compromise, closer scrutiny reveals that this will result in courts being asked to review the adequacy of a country's constitutional guarantees, the relative independence of a country's judiciary and other sensitive questions of foreign government conduct. Because, by excluding the evidence, a judge may feel that he is assuring a conviction for a serious offense, courts may strain to permit the evidence to be introduced, and this may have important, and not necessarily beneficial, foreign policy implications.

Second, it could be argued that since bribery of government officials is universally a crime, Congress should criminalize acts of an American company which run counter to this criminal law policy of foreign nations. Again taking the Middle East as a focus of comparison, it is true that bribery of government officials is considered a crime. The Penal Code of Egypt, for example, forbids a public official to solicit or receive any promise or gift to do or to refrain from doing an act within his jurisdiction.¹⁴⁰ Any violation of the law is punishable by a life sentence at hard labor and a fine of not less than 1000 Egyptian pounds but not more than the value of the promise or the gifts received.¹⁴¹ Saudi Arabian law also prohibits public officials from soliciting or accepting bribes.¹⁴² In addition, the Saudi law criminalizes both payment of the bribe and acting as an intermediary in a bribery transaction.¹⁴³ Violations of the law are punishable by a prison term of up to ten years or a fine not to exceed 20,000 rials.¹⁴⁴ The Kuwaiti statutes prohibit public officials from accepting or soliciting bribes in exchange for the commission or omission of acts within their jurisdiction.¹⁴⁵ The Kuwaiti statute defines public officials to include officials, employees and workers belonging to the government or under its supervision and control.¹⁴⁶ The law of Kuwait provides a jail term of up to ten years for violations of the law.¹⁴⁷ Unlike the Saudi law, in which the prison sentence and fine are stated in the

140. Penal Code of Egypt ch. III, art. 103(b).

141. *Id.*

142. Royal Decree No. 43 of June 16, 1958, art. II (Saudi Arabia).

143. *Id.*

144. *Id.*

145. Law No. 31 of 1970 arts. 35-43 (Kuwait) (amending Law No. 16 of 1960), *reprinted in* Kuwait al Yawm, No. 787, July 26, 1970, at 6-12 [hereinafter cited as Law No. 31 (Kuwait)].

146. *Id.* art. 43(a).

147. *Id.* art. 36.

alternative,¹⁴⁸ Kuwait mandates a fine of double the amount given or promised but not less than 50 Kuwaiti dinars in addition to the prison term.¹⁴⁹ But existing side by side with these statutory proscriptions against bribery is evidence of widespread questionable payments, few investigations of their legality⁵⁰—even in instances where important functionaries seemingly knew of their existence¹⁵¹—and the relatively muted reaction of Middle Eastern governments to the disclosure of these payments. Two conclusions are possible from these facts: (1) the exact parameters of these statutes may never have been tested and, as a consequence, their scope is unclear;¹⁵² or (2) some form of customary law preemption of the written law may have taken place.¹⁵³ Congress would seem less justified in furthering the criminal law policies of foreign nations when from the language of the bribery statutes, it may not be clear that these policies are in fact implicated, or when the foreign nations themselves seem apathetic towards enforcing their own criminal law. Rather, Congress should prescind from criminalizing these payments and, as an alternative, should encourage the executive branch of government to lobby for increased enforcement of foreign bribery laws by the foreign nations themselves. This would have a most salutary effect. If questionable payments are in fact compensating mechanisms for investment protection in certain legal systems, by enforcing their existing bribery statutes, these nations would be required to provide investment protections or risk losing foreign investment. This could only enhance the strength of their respective constitutional guarantees, the independence of their court systems and the effectiveness of arbitration procedures.

III. AMERICAN REGULATORY LAWS

If a comparative legal systems analysis argues against outright criminalization of foreign corporate payments, this same analysis may also prove valuable in considering other American regulatory legislation in this field. At least five distinct sets of statutes relate to the question of corporate payments made to foreign officials. The first set

148. Royal Decree No. 43 of June 16, 1958, art. II (Saudi Arabia).

149. Law No. 31 art. 35 (Kuwait).

150. In 1971, Morocco criminally prosecuted a local agent and four government officials for receiving questionable foreign payments. Report to the Shareholders of the General Tire & Rubber Company, July 19, 1977, at 7. There have been few prosecutions of American companies. See *House Subcommittee Hearings*, *supra* note 126, at 25.

151. See *Senate Subcommittee Hearings*, *supra* note 26, at 847-53.

152. For example, do the statutes cover payments made to a government official to try to influence an act not strictly within his jurisdiction? See text accompanying note 140 *supra*.

153. See generally Brinton, *supra* note 69. A custom or usage is important in the Arabic World. In Egypt, "usage is law." *Id.* at 90. Usage can effectively modify the written law. *Id.*

of statutes—federal and state bribery laws—by their very terms do not specifically cover payments made abroad to foreign officials. Of the four remaining sets, the first two—customs and securities laws—regulate the disclosure of these payments, but not their making. With respect to these laws, the lessons learned from the analysis in Part II will have relevance in determining the extent of disclosure that should be required. The final two groups of statutes—tax and antitrust laws—directly regulate the making of these payments. The comparative legal systems analysis will be relevant in determining whether these payments should be permitted to reduce taxable income or earnings and profits and whether they should be considered anticompetitive acts.

A. *Bribery Laws*

Section 201 of Title 18 of the United States Code prohibits the payment of anything of value to a "public official" to influence official acts.¹⁵⁴ "Public official" is defined as a "Member of Congress . . . or an officer or employee or person acting for or on behalf of the United States, or any department, agency or branch . . . thereof"¹⁵⁵ Similarly, the bribery statute of the State of New York, which is illustrative of state bribery statutes, prohibits payments made to public servants defined as public officers or employees of the State of New York.¹⁵⁶ Thus, the language of both federal and state bribery statutes is limited to bribes paid American, not foreign, officials.

Corporate contributions to foreign candidates or political parties also seem beyond the scope of federal and state law. Section 441b of Title 2 of the United States Code forbids corporate political expenditures or contributions but only in connection with United States presidential or congressional elections.¹⁵⁷ Those state statutes which forbid or regulate corporate political contributions are limited to state elections. Missouri, for example, prohibits any corporation wherever organized from contributing to any political candidate.¹⁵⁸ The wording of the

154. 18 U.S.C. § 201(b) (1970). Violators may be "fined not more than \$20,000 or three times the monetary equivalent of the thing of value, whichever is greater, or imprisoned for not more than fifteen years, or both" *Id.* § 201(e).

155. *Id.* § 201(a).

156. N.Y. Penal Law § 10.00(15) (McKinney 1975). The New York Penal Law makes it unlawful for a "person" to bribe a public servant. *Id.* § 200.00. "Person" is defined as "a human being, and where appropriate, a public or private corporation" *Id.* § 10.00(7). For other state bribery statutes, see, e.g., Mass. Ann. Laws ch. 268A, § 2 (Michie/Law. Co-op 1968); N.J. Stat. Ann. § 2A: 93-6 (West 1969); Va. Code § 18.2-447 (1975).

157. 2 U.S.C. § 441b (1976). *But see* First Nat'l Bank v. Bellotti, 46 U.S.L.W. 4371 (U.S. Apr. 26, 1978).

158. Mo. Ann. Stat. § 130.02Q(5) (Vernon Supp. 1978). Thirty-one states have enacted some form of legislation restricting corporate political activity. First Nat'l Bank v. Bellotti, 46 U.S.L.W. 4371, 4381 n.1 (U.S. Apr. 26, 1978).

statute, however, makes it clear that the prohibition extends only to Missouri elections. Thus, both foreign bribery and foreign political contributions seem beyond the reach of these federal and state bribery statutes.

If federal and state bribery statutes do not cover the making of questionable payments abroad, section 1952 of Title 18 of the United States Code (the so-called "Travel Act") would also seem to have little utility in this area. This section criminalizes travel in interstate or foreign commerce or the use of any facility of interstate or foreign commerce with intent to carry on any unlawful activity.¹⁵⁹ Unlawful activity is defined to include bribery "in violation of the laws of the State in which [it is] committed or of the United States."¹⁶⁰ From the legislative history of the Act, the word "bribery" clearly seems to mean bribery of state, local, and federal officials, not of foreign government officials.¹⁶¹ If, however, the term "bribery" could be construed to cover payments made to foreign officials, the statute still requires that the bribery of the foreign official be "in violation of the laws of the State in which committed or of the United States." At least before passage of the Foreign Corrupt Practices Act, bribery of foreign officials was not specifically criminalized by either state or federal bribery statutes and hence the Travel Act was inapplicable. In order for a prosecutor to have used the Travel Act successfully, he would have had to argue: (a) that, contrary to the legislative history of the section, the word "bribery" could be construed to include bribery of foreign government officials, and (b) that the term "in violation of the laws . . . of the United States" meant "in violation of [any] of the laws . . . of the United States." Since, it can cause anticompetitive effects in the American market, foreign bribery could arguably violate the antitrust laws.¹⁶² Such a reading of the statute seems strained, however. But assuming that a prosecutor could convince a court that the word "bribery" in the Travel Act does cover bribery of foreign officials, the Foreign Corrupt Practices Act could now be used in conjunction with the Travel Act as an alternative basis for indictment.

159. 18 U.S.C. § 1952 (1976). Mail fraud is forbidden by 18 U.S.C. § 1341 (1976). This statute could conceivably be used by the Government to prosecute those companies that have somehow involved the mails in their questionable activities. The difficulty with using this statute is the requirement that it be shown that the payment defrauded someone. The shareholders of the company might be shown to have been defrauded, but an argument that the citizens of the foreign country have been defrauded by the corporate bribe paid to a foreign official seems unsound. But see *N.Y. Times*, Apr. 27, 1978, at 53, col. 5, for a case where one company pleaded guilty to such a charge.

160. 18 U.S.C. § 1952(b) (1976).

161. See *United States v. Brecht*, 540 F.2d 45, 50 n.9 (2d Cir. 1976), *cert. denied*, 429 U.S. 1123 (1977).

162. See pt. III(D) *infra*.

B. *The Bank Secrecy Act of 1970*

Under section 1101 of Title 31 of the United States Code, a person who knowingly transports over \$5,000 in monetary instruments on one occasion either out of, or into, the United States must file a report with the United States Customs Service stating the amount, origin, destination, and route of transportation of the money.¹⁶³ Monetary instruments are defined to include, among other things, currency, travelers' checks, money orders, and bearer negotiable instruments. Order instruments without indorsements are not included within the definition. Wilful failure to file the necessary report is punishable by a \$1,000 fine and/or imprisonment for not more than one year if the amount of money involved is less than \$100,000.¹⁶⁴ For amounts over \$100,000, the penalty for wilful failure to report climbs to a fine of \$5,000 and a possible jail sentence of up to five years.¹⁶⁵ In addition, the law authorizes the imposition of a civil penalty not to exceed the amount of the money which should have been reported.¹⁶⁶ The regulations promulgated under the Act, however, contain one important exception. A transfer of funds through normal banking procedures which does not involve physical transportation of the currency or monetary instrument is not required to be reported.¹⁶⁷

The United States Customs Service is reportedly investigating over one hundred companies that are suspected of secretly transporting money into or out of the United States from corporate slush funds.¹⁶⁸ Some of this money may have been earmarked for making questionable payments to foreign officials. One company and a bank have already been fined for violating the Act's disclosure requirements, although in both of these cases the money was not used to make payments abroad.¹⁶⁹

The thrust of the Bank Secrecy Act is to permit the United States Government to monitor the flow of money into and out of the country. To justify disclosure of these money flows, the United States must

163. Bank Secrecy Act of 1970, 31 U.S.C. § 1101(b) (1970).

164. *Id.* § 1058.

165. *Id.* § 1059.

166. *Id.* § 1103.

167. 31 C.F.R. 103.23 (1977).

168. Jensen, *Customs Service Studies Company Cash Transfers*, N.Y. Times, June 27, 1977, at 41, col. 5. Among the companies under scrutiny are: Lockheed Aircraft Corporation, McDonnell Douglas Corporation, Northrop Corporation, Exxon Corporation, Ashland Oil Inc., and G.D. Searle and Company. *Id.*

169. The company in question was the Gulf Oil Corporation and the bank, the Chemical Bank of New York. N.Y. Times, Nov. 12, 1977, at 27, col. 6. For a Bank Secrecy Act indictment against Deak & Company of California, see N.Y. Times, Oct. 20, 1977, § D, at 3, col. 5. In that case, money was smuggled into the United States. *Id.*

demonstrate that a genuine need for the information exists and that the extent of the disclosure has a reasonable relation to the demonstrated need. In this context, the need for the information is easily demonstrated. The monitoring of international money transactions can be critical in successful narcotics enforcement¹⁷⁰ and in unearthing illicit slush funds. Similarly, in an era of volatile money markets, international money flows can provide the Department of the Treasury with valuable fiscal data. In the light of these needs, the extent of the disclosure required seems reasonable. The origin and destination of the funds are directly related to the national interest in interrupting the narcotics traffic, to cite but one example. To require an American company to disclose cash movements in excess of \$5,000—no matter what their destination—would not seem unjustified under these circumstances.

C. Securities Laws

American securities legislation does not prohibit the making of payments to foreign government officials; it may, however, require their disclosure under appropriate circumstances. However, unlike the need for disclosure under the Bank Secrecy Act—a need which directly relates to the furtherance of the national interest—the need for disclosure of foreign payments under the securities laws rests on a weaker foundation.

Whether information must be disclosed under the securities laws depends upon whether that information is considered "material." Material information has been defined as matter about "which an average prudent investor ought reasonably to be informed before purchasing the security registered."¹⁷¹ The traditional theory has been that the reasonably prudent investor will wish to be kept apprised of those matters which directly affect his investment, that is, financially, as opposed to ethically, material information. In determining whether

170. The Bank Secrecy Act was originally enacted as a weapon against international drug traffic. *N.Y. Times*, Nov. 12, 1977, at 27, col. 6.

171. 17 C.F.R. § 230.405(1) (1977). The term "material" is not defined in either the Securities Act of 1933 or the Securities Exchange Act of 1934. "Material" has, however, been defined generally in regulations. *See, e.g., id.* Recently in construing rule 14a-9, promulgated under § 14a of the Securities Exchange Act of 1934, which deals with proxy solicitations, the Supreme Court adopted a narrow definition of "materiality." An omitted fact in a proxy solicitation is material if there is a substantial likelihood that a reasonable shareholder would—not might—consider it important in deciding how to vote. The definition contemplates a showing of substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the reasonable shareholder's deliberations. *TSC Indus. Inc. v. Northway, Inc.*, 426 U.S. 438, 444-49 (1976). The broader definition of materiality in *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375 (1970) seemingly has been rejected.

corporate payments should be treated as material for disclosure purposes, the comparative legal systems analysis of Part II should be considered.

One justification offered in defense of corporate bribery disclosure is that the payments may reflect on the integrity of company management.¹⁷² If, however, corporate payments in some legal systems act as compensating mechanisms for the lack of other forms of investment guarantees, then, under these circumstances, the making of such payments might not reflect as badly upon management. It has also been suggested that corporate bribery indicates a weak competitive position for the corporation and consequently requires disclosure.¹⁷³ But corporate payments in some countries may be considered more as a hedge against potential arbitrary governmental action, rather than as a sign of a weak competitive position. If anything, the payment of bribes might "be a misleading indicator of [a company's] ability to compete since the extent to which . . . competitors engage in the practice" is unknown.¹⁷⁴ Finally, it has been argued that questionable foreign payments are material because they expose the corporation to contingent liabilities such as foreign criminal prosecution or expropriation.¹⁷⁵ But this argument is perhaps somewhat overstated. In some areas of the world,¹⁷⁶ the relative scarcity of prosecutions seems to indicate that no matter what the letter of the law, the payment may be acceptable in a customary law sense, if not in a statutory law sense.¹⁷⁷ If anything, the disclosure of the payments in the United States might force a foreign government to take action to maintain a certain image of itself in the eyes of the rest of the world.

Beyond the question of whether questionable corporate payments should be considered financially material for disclosure purposes lies perhaps an even more important aspect of SEC policy. Generally, the SEC has requested companies to file undertakings pledging to end future payments.¹⁷⁸ If the conclusions reached in Part II of this Article are accepted, the SEC should carefully consider the consequences of this policy. Requiring "declarations of cessation," may force American companies to operate without the benefit of any compensat-

172. Note, *Disclosure of Payments to Foreign Government Officials Under the Securities Acts*, 89 Harv. L. Rev. 1848, 1857 (1976) [hereinafter cited as *Disclosure*]. On the question of what is material, see also Note, *Foreign Bribes and the Securities Acts' Disclosure Requirements*, 74 Mich. L. Rev. 1222 (1976).

173. *Disclosure*, *supra* note 172, at 1859.

174. *Id.*

175. *Id.* at 1860.

176. See note 150 *supra*.

177. Even in the United States, certain statutes are often invalid indicators of community values. See *Disclosure*, *supra* note 172, at 1858 n.65.

178. See *id.* at 1851, 1861.

ing mechanism against arbitrary government action in a legal system whose very structure creates a greater potential for such arbitrary governmental action.

In deciding such issues, flexible and informed decision-making is required of the SEC. Some disclosure of these payments seems justified, but the extent of that disclosure will be the crucial determination. Perhaps considerations akin to those presented in this Article have already influenced the SEC to adopt a general policy of not requiring identification of the recipient of the bribe even when the payment is deemed material.¹⁷⁹

D. *The Antitrust Laws*

Unlike the customs and securities laws, the antitrust laws apply directly to the making, and not merely to the disclosure, of foreign corporate payments.¹⁸⁰ Section 1 of the Sherman Act prohibits combinations or conspiracies in restraint of trade, while section 2 prohibits monopolization, and attempts and conspiracies to monopolize interstate and foreign commerce.¹⁸¹ Section 5 of the Federal Trade Commission Act forbids unfair methods of competition and unfair trade practices in or affecting foreign as well as interstate commerce.¹⁸² Finally, section 2(c) of the Robinson-Patman Act prohibits payments in connection with a sales transaction except for services rendered.¹⁸³ If these provisions could be given extraterritorial application, a bribe paid to a foreign official by a seller could conceivably violate all three of these statutes.

Although the reach of the Robinson-Patman Act is arguably much narrower than that of the other acts,¹⁸⁴ there is general agreement that the Sherman and Federal Trade Commission Acts will be given extraterritorial effect.¹⁸⁵ In order for the legislation to extend to conduct

179. Report of the Bar of the City of New York, *supra* note 1, at 20.

180. For a more complete analysis of the antitrust considerations with respect to foreign payments, see Rill & Frank, *Antitrust Consequences of United States Corporate Payments to Foreign Officials: Applicability of Section 2(c) of the Robinson-Patman Act and Sections 1 and 2 of the Sherman Act*, 30 Vand. L. Rev. 131 (1977). See also B. Hawk, *International Antitrust* (1978) (in manuscript).

181. 15 U.S.C. §§ 1, 2 (1976).

182. *Id.* § 52.

183. *Id.* § 13(c).

184. See Rill & Frank, *supra* note 180, at 133-37.

185. On the extraterritorial applicability of the Sherman Act, see generally Rill & Frank, *supra* note 180. For the possible extraterritorial use of the Federal Trade Commission Act, see Wall Street J., Oct. 18, 1977, at 2, col. 3. See also, e.g., *Timberlane Lumber Co. v. Bank of America*, 549 F.2d 597 (9th Cir. 1976); *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945).

in a foreign country, however, a showing must be made that, at the least, the foreign conduct had the requisite effect on United States interstate or foreign commerce. For example, if a foreign bribe paid by an American company reduced the chances of a second American company to export its products or acquire part of a foreign market, the necessary showing would presumably be made. However, the antitrust laws recognize certain defenses to otherwise anticompetitive conduct. To determine the scope of these defenses, the comparative legal systems analysis of Part II would seem of particular significance.

1. The Act of State Doctrine

The act of state doctrine "foreclos[es] court adjudications involving the legality of acts of foreign states on their own soil that might embarrass the Executive Branch of our Government in the conduct of our foreign relations."¹⁸⁶ Although the act of state defense is usually claimed by the foreign sovereign, private parties can rely on the defense when their rights are based on, or derived from, an act of the foreign state.¹⁸⁷ The recent Second Circuit case of *Hunt v. Mobil Oil Corp.*,¹⁸⁸ demonstrates how the act of state doctrine might be utilized by an American company induced to pay a bribe by a foreign government official. The majority in *Hunt* found that in order to state an antitrust claim for conspiracy under section 1 of the Sherman Act, plaintiffs would be required to establish that *but for* the defendant's conspiracy, Libya would not have nationalized plaintiff's assets. The court reasoned that in order to establish this causal nexus, the court would be forced to inquire into the acts and conduct of the Libyan Government—an inquiry foreclosed by the act of state doctrine.¹⁸⁹ This same reasoning might apply if an antitrust prosecution were predicated on the paying of foreign bribes. In order to establish an anticompetitive effect in the American market, a showing would have to be made that the foreign government's act in granting a contract or a license was in fact causally linked to the bribe. This inquiry into the motivation of a government's act may be foreclosed by the reasoning in *Hunt*.

To counter the *Hunt* reasoning, one could argue that unlike the formal Libyan nationalization in *Hunt*, a bribe request by a government official is not an act of state since it is not made pursuant to a formal governmental decree or statute.¹⁹⁰ In *Alfred Dunhill of London*,

186. *Alfred Dunhill of London, Inc. v. Cuba*, 425 U.S. 682, 697 (1976).

187. Restatement (Second) of Foreign Relations Law of the United States § 41(3) (1965).

188. 550 F.2d 68 (2d Cir.), cert. denied, 98 S. Ct. 608 (1977).

189. *Id.* at 76.

190. Appellants in *Hunt* emphasized that the lower court noted that the recent disclosures of bribes and payoffs by multinational corporations to foreign officials warranted consideration of

Inc. v. Republic of Cuba,¹⁹¹ a majority of the Supreme Court seemingly required the existence of such a formal decree or statute before the act of state doctrine could apply.¹⁹² Justice Marshall, however, in writing for three other Justices in dissent, argued forcefully against this requirement:

While it is true that an act of state generally takes the form of an executive or legislative step formalized in a decree or measure . . . that is only because duly constituted governments generally act through formal means. When they do not, their acts are no less the acts of a state, and the doctrine, being a practical one, is no less applicable.¹⁹³

When one considers that in some legal systems customary law may in fact preempt statutory law, Justice Marshall's approach seems more in line with the policies underlying the act of state doctrine. If the purpose of the doctrine is to reduce possible judicial interference with the executive's conduct of foreign relations,¹⁹⁴ judicial scrutiny of the customary law acts of a foreign government may involve as much a potential for interference as judicial scrutiny of the statutory law acts of a foreign government.

2. The Defense of Foreign Compulsion

In *Interamerican Refining Corp. v. Texaco Maracaibo, Inc.*,¹⁹⁵ the district court recognized that compulsion by a foreign government can constitute a justification for anticompetitive acts.¹⁹⁶ The rationale stems from the fact that when a foreign nation compels a trade practice, the act becomes in effect not the act of the corporation, but of the foreign nation. The Sherman Act extends only to the trade practices of persons or corporations, not to the trade practices of foreign countries. In order to assess the relevance of the foreign compulsion defense to corporate payments made to government officials in a country whose

the public interest in the continued viability of the act of state doctrine. The Second Circuit refused to reach the issue because there was no allegation that representatives of the Libyan Government "were seduced or enticed in any manner by the payment of bribes or boodle to take the action complained about." 550 F.2d at 79. Thus, until a court reassesses the act of state doctrine in light of the problems presented by questionable payments, the argument presented in the text is not foreclosed. Similarly, the Supreme Court in *Dunhill* has not definitively ruled that the act of state doctrine is unavailable with respect to purely commercial acts of a sovereign.

191. 425 U.S. 682 (1976).

192. "Seemingly" is used because Mr. Justice Stevens seems to agree with the majority opinion that a formal decree or statute must exist before the act of state doctrine can be claimed. *Id.* at 715 (Stevens, J., concurring).

193. *Id.* at 718-19 (Marshall, J., dissenting) (citations omitted).

194. See note 186 *supra* and accompanying text.

195. 307 F. Supp. 1291 (D. Del. 1970).

196. *Id.* at 1298.

legal model is different from that of the United States, assume the following hypothetical situation. American company *X* has a substantial investment in country *Y*. Assume also that a certain minister or government official intimates that the renewal of certain important licenses is contingent upon money payments being made. The clear import of the suggestion is that without the payments there will be no license renewal. Even if the payment could be shown to have anticompetitive effects in the United States, the company may try to justify the payment on the grounds of foreign compulsion.

One commentator has remarked that while direct foreign government compulsion, in the form of a statute or decree, is recognized as a defense: "[t]he law is less clear in regard to conduct which is requested or induced by foreign officials."¹⁹⁷ In order to determine whether informal governmental pressure in a legal system where there is a significant potential for arbitrary action should constitute foreign compulsion, a more detailed analysis of the foreign compulsion defense is required. The Justice Department has highlighted five separate aspects to this foreign compulsion defense.¹⁹⁸ First, the actions compelled must have taken place within the territory of the foreign nation, not within the United States. Second, the corporation must be reasonable in doing what it felt it had to do. Third, the act of compulsion on which the defense is based must be the act of a sovereign entity acting within the scope of its national powers. Fourth, international comity interests must be balanced in deciding whether to treat the act as compelled by the foreign government. Finally, the act of compulsion alleged must relate not to the commercial actions of the foreign government, but only to its public, governmental actions.

Technically of course the payment request by the foreign government official does not meet these five requirements of the foreign compulsion defense. While the act allegedly compelled—the questionable payment—is limited to the territory of the foreign nation and might arguably be viewed as reasonable conduct, particularly in a country without a truly independent judiciary and meaningful constitutional protections against arbitrary government action, the payment would still not meet the final three requirements. But on closer analysis, an argument can be advanced that the payment does meet these three requirements, if not precisely, at least closely enough to permit the defense.

197. Davidow, *Antitrust, Foreign Policy, and International Buying Cooperation*, 84 Yale L.J. 268, 282 (1974).

198. U.S. Dep't of Justice, *Antitrust Guide for International Operations Case L*, reprinted in [1977] *Antitrust & Trade Reg. Rep. (BNA)* E-15 to E-16 [hereinafter cited as *Antitrust Guide*].

a. The Need for a Government Decree

To accede to a bribe request from a foreign government official is not comparable to acceding to conduct mandated by a foreign decree or some other form of duly constituted government action. If anything the letter of the foreign law may actually prohibit the making of these payments.¹⁹⁹ But on the other hand, acceding to the bribe request is not comparable to acceding to the actions of someone who lacks the power to instigate arbitrary action.²⁰⁰ The bribe request from the government official falls somewhere in between these polar points. In a legal system where the statutory forms of the law may not always mirror accepted practices and where the ability to resist arbitrary action is limited, too much emphasis should not be placed on the absence of a formal decree. The fact that alternative means of investment protection may not be available should constitute the bribe request as a form of governmental compulsion sufficient to recognize the defense.

This analysis of course seems to contradict the Supreme Court's holding in *Dunhill* that at least in the case of the act of state doctrine, a formal governmental decree or statute is required to trigger the defense.²⁰¹ But the two defenses (*i.e.* act of state and foreign compulsion) should be kept distinct. The foreign compulsion defense cannot be claimed by a foreign government; it is the defense of the person or company compelled to do something by the foreign government. The litmus test of the defense should be the degree of the compulsion, not the form of the compulsion. From the perspective of the company, it makes little difference whether pressure is exerted by formal decree or statute or by some informal customary practice. Since the company cannot dictate how a government will act, either through formal or informal means, the availability of the defense should not hinge on the method of action chosen by the government.

b. International Comity²⁰²

Recognizing the foreign compulsion defense would not seem to violate international comity, either from the perspective of the foreign

199. See notes 140-49 *supra* and accompanying text.

200. See Antitrust Guide, *supra* note 198, at Case L.

201. 425 U.S. 682, 695 (1976).

202. For a discussion of the considerations that affect an international comity analysis, see Restatement (Second) of Foreign Relations Law of the United States § 40 (1965).

nation or even from the perspective of the United States. Assume a situation where either the bribery statute of country *X* is unclear or the lack of bribery prosecutions suggests that the customary law of the country tolerates corporate payments. Assume also that by making the payment, American corporation *A* keeps its exclusive export market in country *X*, a market to which American corporation *B* might otherwise obtain access. The customary law of country *X* directs one thing, the antitrust law of the United States directs another—namely to refrain from engaging in anticompetitive acts affecting the American export market. Where the laws of two countries conflict, comity requires a balancing of the respective national interests.²⁰³ The interest of the United States in furthering its antitrust policies becomes increasingly weak as the effect of the act on the American market becomes more and more remote. Since the conduct in question takes place almost exclusively within the territory of country *X* and within the accepted parameters of customary law, the interests of country *X* might be at least as strong as the interests of the United States. Unless the payments can be made, American corporations, realizing the lack of other available protections against arbitrary government action in that legal system, may curtail their investments in the country. In effecting this balance, it would not seem inappropriate to consider also the plight of the American company not permitted to use this defense.²⁰⁴ Without it, the American company will be forced to the Hobson's choice of either violating United States law or perhaps foregoing the limited investment security available in another legal system. Balancing the interests of the company and the respective interests of the countries concerned, it is not so clear that comity would require American antitrust principles to prevail.

c. Commercial Versus Governmental Acts

The Antitrust Division of the Department of Justice argues that the availability of the foreign compulsion and act of state defenses should turn on whether the act of the foreign state was governmental or commercial in nature.²⁰⁵ If the act was governmental, the defense applies; if commercial, the defense does not apply. The position of the Antitrust Division seems wrong for several reasons. First, the *Dunhill*

203. See Antitrust Guide, *supra* note 198, at Case L.

204. See Restatement (Second) of Foreign Relations Law of the United States § 40(b) (1965).

205. Antitrust Guide, *supra* note 198, at Case L.

Court was split evenly on the question of whether the act of state defense applies to the commercial acts of a sovereign.²⁰⁶ Mr. Justice Stevens expressed no opinion on this point.²⁰⁷ Thus it is not clear that *Dunhill* makes the commercial versus governmental act dichotomy a controlling distinction. Second, even if the distinction is accepted in act of state cases like *Dunhill*, there are policy reasons against extending the distinction to foreign compulsion cases. The purpose of the act of state doctrine is to reduce judicial interference in the executive's handling of foreign affairs. When the potential for such interference is small as in the case of judicial review of the commercial acts of a foreign government, the defense may be rejected. But the governmental-commercial distinction makes little sense in foreign compulsion cases where the defense is based on coercion. If a foreign official requests a bribe, whether in relation to the performance of a governmental or commercial act, the degree of compulsion is the same. Even if a court held that the foreign compulsion defense did not apply to the commercial acts of a foreign government, it would be difficult to make precise distinctions in this area.²⁰⁸ Many of the acts for which a bribe might be requested are not easily classified as either governmental or commercial. For example, the renewal of an export or import license, exchange control permissions, and the grant of working permits for foreign employees would all seem to be governmental acts. Less clear, however, would be the decision to buy one type of military aircraft over another.

3. The *Noerr-Pennington* Doctrine

The *Noerr-Pennington* doctrine²⁰⁹ immunizes from antitrust attack activities aimed at the solicitation of governmental action with respect to the passage, enforcement and administration of laws, even if the purpose of the solicitation was anticompetitive in nature and accompanied by deception of public officials. The doctrine is based in part on the constitutional right of petition²¹⁰ and as a consequence, one court has

206. 425 U.S. 682 (1976).

207. *Id.* at 715 (Stevens, J., concurring).

208. The Antitrust Division itself recognizes this. See Antitrust Guide, *supra* note 198, at E-15 n.98.

209. *United Mine Workers v. Pennington*, 381 U.S. 657 (1965); *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961).

210. *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 138 (1961). The *Noerr-Pennington* doctrine has been applied to dealings with the legislature, see *Noerr*, *supra*, the executive, see *United Mine Workers v. Pennington*, 381 U.S. 657 (1965), and

stated in dictum that the doctrine does not apply readily to petitioning foreign governments.²¹¹ The Antitrust Division of the Department of Justice, however, has taken a contrary position, arguing "that private representations to a foreign government leading to action of that government restraining United States foreign commerce is within the protection of the *Noerr-Pennington* doctrine."²¹² If an American company bribes a foreign official to encourage the enactment of a government regulation which would adversely affect other American companies, could such conduct be protected by the *Noerr-Pennington* doctrine? Relying on dictum in *California Motor Transport Co. v. Trucking Unltd.*²¹³ and a number of lower court decisions, "the Antitrust Division has noted that the *Noerr-Pennington* defense may not apply where the representations are accompanied by bribery."²¹⁴ The legality of the payment under the applicable foreign law would seem to be a determinative factor, since the *Noerr-Pennington* doctrine, although it may protect deliberate deception, should not be extended to protect illegal conduct. But often the bribery laws of a foreign country may be unclear. Even when clear, by accepting the distinction between what is formally legal and what is accepted by custom, a company may try to argue that in a practical sense bribery should be considered at worst unethical, but not illegal, conduct.

E. Tax Laws

The last set of statutes that relate to the legality of foreign corporate payments are the tax laws. Before 1958, the deductibility of questionable foreign payments made by corporations was generally regulated by case law.²¹⁵ Even though such payments might arguably have been

the courts, see *Otter Tail Power Co. v. United States*, 419 U.S. 366, 379-80 (1973). Similarly, the doctrine has been extended to dealings with administrative agencies, the fourth branch of government. See *California Motor Transp. Co. v. Trucking Unltd.*, 404 U.S. 508, 513 (1972).

211. *Occidental Petroleum Corp. v. Buttes Gas & Oil Co.*, 331 F. Supp. 92, 107-08 (C.D. Cal. 1971) (dictum), *aff'd*, 461 F.2d 1261 (9th Cir.), *cert. denied*, 409 U.S. 950 (1972).

212. Report of the Bar of the City of New York, *supra* note 1, at 25; Antitrust Guide, *supra* note 198, at Case N.

213. 404 U.S. 508 (1972). The lower court decisions are: *Sacramento Coca-Cola Bottling Co. v. Teamsters Local 150*, 440 F.2d 1096 (9th Cir. 1971), *cert. denied*, 404 U.S. 826 (1972); *Woods Exploration & Producing Co. v. Aluminum Co. of America*, 438 F.2d 1286 (5th Cir. 1971), *cert. denied*, 404 U.S. 1047 (1972); *Marketing Assistance Plan, Inc. v. Associated Milk Producers, Inc.*, 338 F. Supp. 1019 (S.D. Tex. 1972).

214. Report of the Bar of the City of New York, *supra* note 1, at 25.

215. B. Bittker & J. Eustice, *Federal Income Taxation of Corporations and Shareholders* 7-19 n.34 (1971).

considered "ordinary and necessary" business expenses, the courts consistently held that illegal payments were non-deductible because they frustrated public policy.²¹⁶ In 1958, Congress amended section 162 of the Internal Revenue Code²¹⁷ to reflect this "frustration of public policy" approach taken by the courts. The language of the amendment prohibited the deduction of payments made to an official or an employee of a foreign government where such payments would have been unlawful under the laws of the United States had such laws applied.²¹⁸ Although the phrase "payment made, directly or indirectly, to an official . . . of a foreign country" was not defined in the statute, the language seemed sufficiently broad to encompass most forms of these payments.²¹⁹ Furthermore, the regulations make it clear that such payments would be disallowed even though the payments were legal under the law of the country where they were made.²²⁰ This provision of course concerns not the legality under American law of payments made to foreign officials, but their deductibility in computing taxable income. As long as these payments were not deducted in arriving at taxable income, there is no violation of section 162.

Of course, an extreme reading of the comparative analysis developed in this article could be used to challenge the Internal Revenue Code's position as to the deductibility of foreign corporate payments in arriving at taxable income. Since in certain legal systems, these payments may sometimes be a form of compensating mechanism against arbitrary government action, they might be justified as an ordinary and necessary business expense. But because many of these payments, even in such legal systems, may not be inspired by investment-protection motives, it may be justifiable to disallow all such payments from an

216. *Id.*

217. Technical Amendments Act of 1958, Pub. L. No. 85-866, § 5(a), 72 Stat. 1608 (1958).

218. I.R.C. § 162(c)(1). For a reference to an Internal Revenue Service inquiry into the foreign payments practices of one company, see N.Y. Times, Mar. 31, 1978, § D, at 1, col. 2.

219. In 1969, § 162(c) was further amended to read: "(c) Illegal bribes, kickbacks and other payments.—(1) Illegal payments to government officials or employees.—No deduction shall be allowed under subsection (a) for any payment made, directly or indirectly, to an official or employee of any government, or of any agency or instrumentality of any government, if the payment constitutes an illegal bribe or kickback or, if the payment is to an official or employee of a foreign government, the payment would be unlawful under the laws of the United States if such laws were applicable to such payment and to such official or employee. The burden of proof in respect of the issue, for the purposes of this paragraph, as to whether a payment constitutes an illegal bribe or kickback (or would be unlawful under the laws of the United States) shall be upon the Secretary to the same extent as he bears the burden of proof under section 7454 (concerning the burden of proof when the issue relates to fraud)." I.R.C. § 162(c).

220. Treas. Reg. § 1.162-18(a)(ii) (1970).

administrative standpoint. If the rule were otherwise, there would be the possibility that some corrupt payments would be used successfully to reduce taxable income, thus permitting a corrupt payment to have a direct and immediate effect on the revenues collected.

But it is not as clear that the same administrative rule should prevail where taking account of these payments would not have as immediate and direct an effect on the amount of revenues collected. Under these circumstances, there would seem to be room to balance other considerations in fashioning the applicable rule. Earnings and profits is an accounting concept which determines whether a corporate distribution is a dividend which is taxable income to the shareholder or a return of capital which reduces the shareholder's basis in his stock.²²¹ In certain situations a payment which cannot be deducted in determining taxable income can be deducted in computing earnings and profits.²²² Penalties for tax fraud are one such item.²²³ In determining earnings and profits, it is less clear how foreign payments should be treated. From a purely accounting standpoint, it makes sense to reduce earnings and profits by the amount of the questionable payments in order to picture accurately the economic position of the company. But, by permitting an American parent company to reduce earnings and profits, there could be an indirect reduction in the amount of tax revenue collected. When earnings and profits are reduced, the amount taxed as a dividend on distribution may similarly be reduced. Thus, the Internal Revenue Service (IRS) may lose potential revenue because there will be less taxable dividends distributed to the shareholders. Although as a practical matter most large companies often carry forward enough retained earnings and profits to make all distributions dividends, is the theoretical possibility of reduced tax revenue sufficiently strong to outweigh the definite accounting advantages in permitting the reduction of earnings and profits? If American public policy of a non-tax nature was frustrated by permitting the reduction, the answer to the question might be yes. But the various non-tax policies at stake are not clearly thwarted by permitting the reduction. It could be argued, for example, that foreign corporate payments could lead to confrontations between the United States and foreign nations. In countries where prosecutions for these payments have been rare,²²⁴ the chance for

221. Bittker & Eustice, *supra* note 215, at 7-9 to 7-20.

222. *Id.* at 7-18 to 7-20.

223. Rev. Rul. 57-332, 1957-2 C.B. 231. *But see* Bernstein v. United States, 234 F.2d 475 (5th Cir.), *cert. denied*, 352 U.S. 915 (1956).

224. *See* note 150 *supra*.

serious confrontation seems unlikely. If the argument is made that the United States should disallow the earnings and profits reduction on moral grounds, on the theory that these payments ultimately corrupt the maker as well as the recipient, one should recall that a "corrupt" motive may not be the only reason for making these payments in other legal systems. Similarly, although questionable payments to foreign officials may spawn slush funds or other unethical corporate practices, permitting the reduction might disclose these practices faster than a rule which does not permit the reduction.

In Revenue Ruling 77-442, the IRS has agreed that at least as to payments made to foreign government officials before November 3, 1976, earnings and profits can be reduced by the amount of the payments, both for the American parent corporation and for any of its foreign subsidiaries.²²⁵ But, because of a 1976 amendment to section 964(a) of the Internal Revenue Code,²²⁶ the rule has been changed for foreign subsidiaries of American parent corporations, at least with respect to computing the earnings and profits of these foreign subsidiaries for purposes of subpart F, part III, subchapter N, chapter I of the Code. Presumably, in all other circumstances, earnings and profits can still be reduced by the amount of any questionable payments. For the reasons stated above, the amendment to section 964(a) does not seem a wise decision.

IV. CONCLUSION

This Article has not been written as a definitive answer to the question of how Congress should regulate the serious problem of foreign questionable payments. Rather, it has been written to sharpen the focus on only one aspect of the problem: the comparative law considerations raised by criminalizing these questionable payments. Because of the seeming dissimilarities that exist between the American legal model and those legal models that exist in certain other areas of the world, this Article has argued against criminalization. Perhaps the regulatory controls that existed prior to passage of the Foreign Corrupt Practices Act, if carefully and judiciously enforced, may better serve the American national interest. But by emphasizing only one aspect of the problem, this Article has necessarily prescinded from a discussion of those other policy reasons supporting criminalization of foreign

225. Rev. Rul. 77-442, 1977-48 I.R.B. 10.

226. Tax Reform Act of 1976, Pub. L. No. 94-455, § 1065(b), 90 Stat. 1654 (1976) (codified at I.R.C. § 964(a)).

payments. The most critical of these other policy reasons is, of course, morality. It is clear that these payments, if made in the United States would be both illegal and morally repugnant to the vast majority of Americans. Whether these moral standards should, by statute, be given extraterritorial application to Americans living and working in divergent cultures is a question with strong jurisprudential overtones. In the Foreign Corrupt Practices Act, Congress itself grappled with this problem and made something of an accommodation, by deciding to criminalize outright bribes but not the so-called "grease" payments. The question of whether, or to what extent, an accommodation should be made to different cultures will undoubtedly spawn an interesting body of jurisprudential literature.